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Abusive Tax Shelters, Legal Malpractice, and Revised Formal Ethics Opinion 346: Does Revised 346 Enable Third Party Investors to Recover From Tax Attorneys Who Violate Its Standards?

Joseph J. Portuondo*

No group of individuals . . . can be permitted by adopting careless and slipshod methods to save time, effort, or money, to set its own uncontrolled standard at the expense of the rest of the community. If the only test is to be what has always been done, no one will ever have any great incentive to make any progress in the direction of safety.¹

The organized bar has conceded that many attorneys issue tax shelter opinions of questionable ethical standards.² Indeed, some have remarked that “the perception . . . that sham and corner cutting in the tax shelter area is an acceptable and customary part of tax practice” poses a “threat to the profession.”³

Revised Formal Ethics Opinion 346 (Revised 346),⁴ issued by the American Bar Association (ABA) Committee on Ethics and Professional Responsibility on January 29, 1982, is the organized bar’s repudiation of and answer to this improper practice. Revised 346 clearly articulates the committee’s perception of what constitutes appropriate conduct for lawyers working in the tax shelter opinion area.⁵

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¹ R. Malen & V. Levent, Legal Malpractice 339 n.8 (2d ed. 1981) (citing Restatement (Second) of Torts § 295A comment e (1965)).
⁵ “[C]oncerns have been expressed by the organized bar, regulatory agencies, and others over the need to articulate ethical standards applicable to a lawyer who issues [a tax shelter] opinion.” Revised 346, supra note 4, at 1.

A responsibility of the committee is to express its opinion on proper professional conduct of lawyers and to do so by a formal opinion where the subject is of widespread interest [citation omitted]. Accordingly, the committee expresses its opinions as to the standard applicable to lawyers who issue tax shelter opinions.
The ABA Standing Committee on Ethics and Professional Responsibility was faced with the threat of government regulation, and frustrated by the undoubtedly unethical practices of attorneys who provide opinions which promote abusive tax shelters. Revised 346, the ABA response, sets forth appropriate professional standards which lawyers should follow when rendering tax shelter opinions. However, despite its issuance, and a warning that the ABA will cooperate with the Internal Revenue Service (IRS) in referring violations to disciplinary agencies, attorneys continue to participate in these abuses.

Although the use of ethical standards to achieve compliance with the tax laws appears to be a relatively new concept, courts often use ethical standards in measuring an attorney's liability for legal malpractice. Although investors have not yet employed Revised 346 to define an attorney's liability for legal malpractice when their tax shelters fail, a strong argument for doing so exists.

This article examines the potential use of Revised 346 in these cases. Part I reviews the background of the problem which prompted the ABA's issuance of Revised 346, and Part II discusses the standards which Revised 346 sets. Part III argues that Revised 346 establishes that investors can sue as third party beneficiaries, or at least, that Revised 346 sets the applicable standards in such suits. Finally, Part IV details the elemental ramifications

Id. at 2.

[T]hese canons and ethical considerations constitute a body of principles which provide guidance in the application of the lawyer's professional responsibility to specific situations, such as the rendering of tax shelter opinions.

Id. at 4.

6 See note 5 supra and notes 33-47 infra and accompanying text.

7 The term "tax shelter" is generally used to describe an investment which permits an investor to benefit from a deduction or credit which operates to reduce or "shelter" taxable income from other sources. An abusive tax shelter is one which purports to qualify for legitimate tax benefits but which in fact does not qualify.

8 ABA Tax Section Rails Against Tax Shelters, 23 TAX NOTES 1018, 1019 (1984).

9 "Despite efforts by the ABA to use ABA Ethics Opinion 346 to discourage opinion letters for abusive tax shelters, representatives from the IRS tax shelter program told the [IRS Commissioner's] advisory group that the tax shelter promotions continue." IRS May Work With Securities Agencies, ABA on Tax Shelters, 20 TAX NOTES 829 (1983). Although ABA Ethics Opinion 346 requires that attorneys who write tax shelter opinion letters determine if the tax shelter's appraiser is qualified and if the appraisal appears reasonable on its face, it appears that many attorneys accept the appraisal that is provided to them, and thus the substance of the tax shelter transaction has not changed. Id. See also note 45 infra.


11 See text accompanying notes 16-50 infra.

12 See text accompanying notes 51-82 infra.

13 See text accompanying notes 83-116 infra.

14 See text accompanying notes 117-42 infra.
of Revised 346's applicability to legal malpractice cases.\(^{15}\)

**I. The Nature of the Problem and Reaction to Abusive Tax Shelter Practices**

The IRS began attacking abusive tax shelters early in the 1970's and since then has continued to do so with ever increasing intensity. Initially the IRS focused on the question of whether it should recognize (for tax purposes) organizations constituted as partnerships as such, or, whether it should classify such entities as associations taxable as corporations, thereby eliminating the essential feature permitting the sheltering of income.\(^{16}\) These attacks began with the issuance of revenue procedures designed to create artificial operating rules under which the IRS could deny advanced revenue rulings to many tax shelter arrangements.\(^{17}\) However, tax practitioners uniformly recognized that the IRS could not support its position in these revenue procedures and, consequently, they routinely ignored them.\(^{18}\)

The Tax Reform Act of 1976 succeeded, to some degree, in curbing the use of abusive tax shelters by introducing "at risk" rules, the capitalization requirement of construction period interest and taxes,\(^{19}\) and stricter rules regarding the use of special and retroactive partnership allocations.\(^{20}\) The IRS continued its attack on October 31, 1977, by issuing the famous "Halloween Massacre" rulings.\(^{21}\) These rulings presented an aggressive and expansive interpretation of the "at risk" rules. The Revenue Act of 1978 extended the "at risk" rules even further.\(^{22}\)

The IRS then shifted its strategy by questioning overvaluations.\(^{23}\) In Rev. Rul. 77-110, the IRS held that if the amount of a nonrecourse debt incurred to purchase property exceeded the value of the property, then no amount of the debt could be in-

\(^{15}\) See text accompanying notes 143-81 infra.


\(^{17}\) Rev. Proc. 72-13, 1982-1 C.B. 735; Rev. Proc. 74-17, 1974-1 C.B. 438.


\(^{23}\) Some abusive tax shelters have involved overvaluations between 200 and 400 percent. LeDuc, *The Legislative Response of the 97th Congress to Tax Shelters, the Audit Lottery, and Other Forms of Intentional or Reckless Noncompliance*, 18 TAX NOTES 363, 371 (1983).
cluded in basis. This precluded the use of a number of abusive tax shelters. The overvaluation fight continued in the “Saint Patrick’s Day Massacre” of March 17, 1980, when the IRS issued several rulings concerning the permissibility of deductions, the valuation of property contributed to charity, the classification of an entity for tax purposes, sham transactions, and the “at risk” rules. Again, the effect was a constriction of the abusive tax shelter market.

The Economic Recovery Tax Act of 1981 (ERTA) shut down a large area of tax shelter activity by eliminating the very controversial and unwarranted tax advantages of commodity straddles. ERTA also introduced new penalties for income tax underpayments attributable to substantial valuation overstatements. However, the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) provided an even greater legislative effort to curb abuses. TEFRA addressed the problem of abusive tax shelters and the related audit lottery by imposing penalties on investors and promoters, and by providing courts with injunctive authority to deal with repeat offenders.

But these efforts to curb abuses were not successful in combating the increasing problem of abusive tax shelters. On January 15, 1980, the Commissioner of Internal Revenue stated that the IRS was investigating 200,000 individual income tax returns involving approximately 18,000 tax shelter schemes and about $5 billion dollars in questionable deductions. The Commissioner further

30 The term “audit lottery” refers to the ability of a taxpayer to take undisclosed aggressive positions in his return with little fear of an audit and less fear of the imposition of penalties because the IRS reviews relatively few tax returns and assesses even fewer deficiencies.
33 Kurtz, The State of Our Federal Tax System, S. CAL. L. CENTER THIRTY-SECOND ANNUAL INST. ON FEDERAL TAX’N 17-9 (1980). This is a small percentage of the estimated $100 billion lost annually due to taxpayer noncompliance. LeDuc, supra note 23, at 370. However, the existence of abusive tax shelters involving outrageous contrivances reinforces the popular belief in taxpayer inequality and tax law inequity. These perceptions lead to an across the board decline in voluntary compliance with the tax laws. Sax, Lawyer Responsibility in Tax Shelter Opinions, 34 Tax Law. 5 (1980); Note, Ethics Ruling on Legal Opinions in Tax Shelter Investment Offerings, 7 Del. J. Corp. L. 449, 450 (1982). Taxpayer noncompliance
stated that many abusive tax shelters depended upon the participation of tax attorneys for their successful marketing34 and that the IRS was exploring the "ethical and legal standards which should govern" attorneys' conduct in these schemes.35 Only three days later, the General Counsel of the Treasury Department echoed the Treasury's concern regarding tax attorneys who "through their opinions control access to the tax shelter marketplace."36 The General Counsel identified several types of opinions which were considered "abusive": the false opinion,37 the assumed facts opinion,38 the non-opinion,39 and the reasonable basis opinion.40 He warned that the Treasury Department would invoke its statutory authority41 to discipline attorneys who pen abusive tax shelter opinions unless the organized bar accepted the responsibility of regulating the practice.42

This warning became reality on September 3, 1980, when the IRS issued proposed amendments to Circular 23043 setting forth stricter standards of conduct for attorneys who provide tax shelter

leads to economic inefficiencies as well. The litigation explosion (and all the wasted resources such litigation involves) has penetrated the tax court. In April 1981 there were 36,246 cases pending before the tax court of which an estimated 2,500 to 3,000 were tax shelter cases. Id. at 449. Recently, the tax court had approximately 57,000 cases pending of which 20,000 were tax shelter cases. ABA Tax Section Rails Against Tax Shelters, supra note 8, at 1019.

34 Tax opinions play a crucial role in the promotion and marketing of tax shelters. LeDuc, supra note 23, at 381; Sax, supra note 33, at 14-16; see ABA Section on Taxation, Statement on Proposed Rule Amending Circular 230 With Respect to Tax Shelter Opinions, 34 Tax Law. 745 (1981). Tax opinions began to play this important role in tax avoidance in the 1950's. LeDuc, supra note 23, at 388. See also Brown, Advice of Tax Adviser as Insulation Against Penalties, S. CAL. L. CENTER THIRD ANNUAL INST. ON FEDERAL TAX'N 497 (1951). Revised 346, supra note 4, at 1, explicitly recognizes that "the successful marketing of tax shelters frequently involves tax opinions."

35 Kurtz, supra note 33, at 17-10.

36 Report by the Tax Section of the New York State Bar Ass'n, Circular 230 and the Standards Applicable to Tax Shelter Opinions, 12 Tax Notes 251, 253 (1981) (quoting Robert H. Mundheim, General Counsel of the Treasury Department, speaking at the Securities Regulation Institute on Jan. 18, 1980) [hereinafter cited as Mundheim].

37 A "false opinion" is one which omits serious legal risks and knowingly or recklessly misstates facts or law. Mundheim, supra note 36, at 255.

38 An "assumed facts opinion" is one which relies upon underlying facts but disclaims any knowledge of the accuracy of those facts. Mundheim, supra note 36, at 255-56.

39 A "non-opinion" discusses hypothetical facts and legal issues but never relates the law to the actual facts. Mundheim, supra note 36, at 256.

40 A "reasonable basis opinion" states a reasonable basis for claiming tax benefits without predicting the outcome. In some instances, these opinions actually predict that the taxpayer benefits will not materialize. Mundheim, supra note 36, at 256-58.


42 Mundheim, supra note 36, at 259.

opinions. As amended, Circular 230 provided that the failure to adhere to the announced standards could in some situations result in suspension or disbarment from practicing before the IRS. The IRS reproposed these amendments (with modifications) on December 15, 1982, and on February 27, 1984, they were finalized.

The bar’s initial reaction was unsurprisingly critical. Accordingly, on June 1, 1981, the ABA Standing Committee on Ethics and Professional Responsibility responded by issuing Formal Ethics Opinion 346, which details ethical conduct standards for attorneys in the tax shelter area. A number of groups suggested modifications, and on January 29, 1982, Revised 346 superseded Opinion 346.

II. The Standards of Revised 346

A legal savant has been quoted as saying that “the lawyer obtains as much precise direction from his guide to professional responsibility as a heart surgeon could usefully derive from examination of a valentine.” Indeed, most rules of ethics provide little guidance because their language is too general, if not obtuse. Atypically, Revised 346 contains rather specific standards to guide

45 Commentators disagree about the effectiveness and severity of this punishment. Some have remarked that violations of Circular 230 “will expose the person charged with a most serious loss, the right to practice his profession before the I.R.S.” Goldfein & Weiss, An Analysis of the Proposed Changes Under Circular 230 Affecting Tax Shelter Opinions, 53 J. Tax’n 340 (1980). However, another author persuasively argues that:

[T]o many lawyers who would write a tax shelter opinion the threat of discipline is empty. Loss of the right to practice before the service is the forfeiture of the right to participate in the letter rulings process and to represent taxpayers in administrative disputes. For most lawyers these rights have little practical significance. Legal practices may develop that are devoted to giving tax shelter opinions free of concern for discipline, because giving opinions does not constitute “practice before” the service . . . .

Sax, supra note 33, at 45.
46 Prop. Regs. §§ 10.2(a), 10.7(c), 10.33, 10.51(j), 10.52, 10.76, 47 Fed. Reg. 56,144 (1982) (codified at 31 C.F.R. §§ 10.2(a), 10.7(c), 10.33, 10.51(j), 10.52, 10.76).
47 These regulations are effective for opinions issued after Feb. 23, 1984. 31 C.F.R. § 10 (1984). They also contain standards which are substantially similar to those of Revised 346. See notes 51-82 infra and accompanying text.
48 See Schlenger, supra note 16; ABA Section on Taxation, supra note 34; Goldfein & Weiss, supra note 45.
50 See note 4 supra.
52 Although guidelines set forth in Revised 346 under “Ethical Considerations” are directory in nature, this article treats them as mandatory because courts have made no distinction between mandatory and aspirational rules of ethics in legal malpractice actions. See cases cited in note 130 infra. See also note 98 infra.
attorneys in rendering tax shelter opinions.\textsuperscript{53}

Revised 346 requires an attorney to establish the terms of his relationship with his offeror-client at the outset, and to make clear to the client that he requires full disclosure of the structure and intended operation of the venture upon which he will render an opinion.\textsuperscript{54} The attorney is further directed to require the client to provide complete access to all relevant information.\textsuperscript{55}

Revised 346 also incorporates by reference the guidelines stated in ABA Formal Opinion 335.\textsuperscript{56} This opinion sets the standards which attorneys should follow in determining the relevant facts which underlie the transaction upon which they will issue a tax shelter opinion.\textsuperscript{57} Under these standards, an attorney first of all must ask his client for all the relevant facts. If his inquiry produces facts which are "incomplete in material respect, . . . suspect, or . . . inconsistent either on their face or on the basis of other known facts,"\textsuperscript{58} the attorney must then inquire further. The extent of this inquiry will depend upon the circumstances of each particular case. If the facts as related by the client are neither inconsistent nor suspect, then the attorney may presume that they are accurate.\textsuperscript{59} In this regard, Revised 346 emphasizes that the attorney must be particularly cautious when evaluating appraisals and financial projections relating to tax shelter arrangements.\textsuperscript{60}

\textsuperscript{53} A "tax shelter opinion" for purposes of Revised 346 is defined as "advice by a lawyer concerning the federal tax law applicable to a tax shelter if the advice is referred to either in offering materials or in connection with sales promotion efforts directed to persons other than the client who engages the lawyer to give advice." Revised 346, supra note 4, at 2. A "tax shelter" for purposes of Revised 346 is an investment which offers significant benefits to investors in either or both of the following ways: For federal income tax or excise tax purposes, the investment provides deductions in excess of income, thereby reducing income from other sources in a given year; or, the investment provides credits in excess of the tax attributable to income in a given year, thereby offsetting taxes from other sources. \textit{Id.} at 2 n.1.

\textsuperscript{54} \textit{Id.} at 5.

\textsuperscript{55} \textit{Id.}

\textsuperscript{56} ABA Comm. on Ethics and Professional Responsibility, Formal Op. 335 (1974) [hereinafter cited as Opinion 335].

\textsuperscript{57} Revised 346, supra note 4, at 5; Opinion 335, supra note 56, at 5.

\textsuperscript{58} Revised 346, supra note 4, at 5 (quoting Opinion 335, supra note 56, at 5).

\textsuperscript{59} The essence of [Opinion 335] . . . is that, while a lawyer should make adequate preparation including inquiry into the relevant facts . . . and while he should not accept as true that which he should not reasonably believe to be true, he does not have the responsibility to "audit" the affairs of his client or to assume, without reasonable cause, that a client's statement of the facts cannot be relied upon.

\textsuperscript{60} Revised 346, supra note 4, at 5 (citing Opinion 335, supra note 56, at 3, 5-6).

For instance, where essential underlying information, such as an appraisal or financial projection, makes little common sense, or where the reputation or expertise of the person who has prepared the appraisal or projection is dubious, further inquiry clearly is required. Indeed, failure to make further inquiry may result in a false opinion. [See note 37 supra.] If further inquiry reveals that the appraisal or
Revised 346 further requires attorneys rendering tax shelter opinions to relate the law to the actual facts of the transaction to the extent that the facts are then ascertainable.\textsuperscript{61} Although he may assume facts which are not ascertainable at that time, the attorney must clearly identify those facts as assumed.\textsuperscript{62} However, in no event can an attorney issue an opinion which "disclaims responsibility for inquiring as to the accuracy of the facts, fails to analyze critical facts, or discusses purely hypothetical facts."\textsuperscript{63}

Revised 346 also imposes a new obligation upon tax shelter attorneys to make "reasonable inquiries" to ascertain whether the client has expended a "good faith effort" to comply with laws other than the tax laws.\textsuperscript{64} The attorney must do this even though the client has not asked him to address such issues.\textsuperscript{65} However, in doing so, the attorney need not reexamine the conclusions of other counsel. He must simply satisfy himself that the client obtained competent professional advice on those issues.\textsuperscript{66}

Perhaps the most important requirement of Revised 346 is that the attorney must take reasonable steps to ensure that either he or other counsel has considered all material\textsuperscript{67} federal income and exercise tax issues.\textsuperscript{68} If an issue involves "a reasonable possibility that the [IRS] will challenge the tax effect proposed in the offering materials," then the attorney must address such an issue "fully and fairly."\textsuperscript{69} If other professionals are considering the same material tax issues, the attorney must review their written advice and take steps to ensure that "the division of responsibility as to the issues is clear and . . . that all material tax issues will be considered . . . \textit{in accordance with the standards}" of Revised 346.\textsuperscript{70} Should the attorney find that no one has adequately addressed an issue which the IRS may contest, he must then inform the client and the other counsel that the projection is reasonably well supported and complete, the lawyer is justified in relying upon material facts which the underlying information supports.

\textit{Id.}
\textsuperscript{61} \textit{Id. at 6.}
\textsuperscript{62} \textit{Id.}
\textsuperscript{63} \textit{Id.}
\textsuperscript{64} \textit{Id.}
\textsuperscript{65} \textit{Id.}
\textsuperscript{66} \textit{Id.}
\textsuperscript{67} A "material tax issue" for purposes of Revised 346 is one which would have a "significant effect in sheltering from federal taxes income from other sources by providing deductions in excess of the income from the tax shelter investment in any year or tax credits which will offset tax liabilities in excess of the tax attributable to the tax shelter investment in any year." \textit{Id.} The attorney determines what is material by making a good faith analysis of information then available. \textit{Id.}
\textsuperscript{68} \textit{Id. at 7.}
\textsuperscript{69} \textit{Id.}
\textsuperscript{70} \textit{Id. (emphasis added).}
of that fact. Furthermore, he must refuse to provide an opinion until the matter is corrected.

In addition, the attorney must state his opinion as to the probable outcome of each material tax issue. However, he need not do this if in good faith he cannot make that judgment. The attorney must also provide an overall evaluation as to the extent to which "tax benefits, in the aggregate, which are a significant feature of the investment to the typical investor, are likely to be realized." Revised 346 assumes that only in "rare" instances will an attorney be unable to make a good faith overall evaluation of the potential benefits. In these instances, Revised 346 requires a full explanation as to why the attorney could not make this evaluation.

Where the attorney's evaluation reveals that the tax sheltering effect is dubious, Revised 346 permits tax shelter opinions which conclude that clients will probably not realize significant tax benefits. However, the attorney must clearly state and prominently note this conclusion in the offering materials. The attorney must be especially careful not to mislead investors when he issues a negative opinion.

Finally, Revised 346 also requires that the offering materials represent the true nature and full extent of the tax shelter opinion. If the attorney cannot agree with the client over the extent of this disclosure, he is under an ethical duty to withdraw from employment and not issue the opinion.

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71 Id.
72 Id. "The lawyer also should assure that his own opinion identifies clearly its limited nature, if the lawyer is not retained to consider all of the material tax issues." Id.
73 Id.
74 Id.
75 Id. at 8.
76 Id. "This impossibility may occur where, for example, the most significant tax benefits are predicated upon a newly enacted Code provision where there are no regulations and the legislative history is obscure." Id.
77 Id. The attorney must also provide "full disclosure in the offering materials of the assumptions and risks which the investors must evaluate." Id.
78 Id. These are referred to as "negative conclusions."
79 Id. The continued usefulness of negative or reasonable basis opinions, see note 40 supra, is doubtful because they no longer insulate investors from penalties. See LeDuc, supra note 23, at 369-74. Indeed, an attorney issuing such opinions, which result in the imposition of penalties on investors, is per se negligent.
80 Revised 346, supra note 4, at 8-9.
81 Id.
82 If the lawyer disagrees with the client over the extent of disclosure made in the offering materials or over other matters necessary to satisfy the lawyer's ethical responsibilities as expressed in [Revised 346], and the disagreement cannot be resolved, the lawyer should withdraw from employment and not issue an opinion.

Id. at 9.
III. Applicability of Revised 346 in Tax Shelter Malpractice Actions

A. Overview of Legal Malpractice

Legal malpractice occurs when an attorney fails to use such skill, prudence, and diligence as lawyers of ordinary skill and capacity commonly possess and exercise in the performance of their clients' work. In any legal malpractice action, the plaintiff must prove by a preponderance of the evidence that the attorney owes him a duty of care, that the duty was breached by the attorney's failure to use reasonable care and skill, and that the breach of the duty was the proximate cause of the plaintiff's damages.

In recent years dissatisfied clients and third party beneficiaries have brought an increasingly large number of legal malpractice actions against attorneys. One commentator has remarked that the "increasing incidence of recoveries against attorneys for malpractice" constitutes a "legal revolution." In addition to actions against attorneys for simple negligence, these legal malpractice actions are often cast in terms of breach of fiduciary duty, breach of express or implied contract, and fraud.

B. The Duty of Care Owed to Investors Under Revised 346

1. The Traditional Rule

An attorney is liable for legal malpractice only to those to whom he owes a duty of care. Traditionally, courts held that an attorney owed a duty only to those to whom he was in privity—namely, his client. As a result, the widely accepted rule was that a non-client investor could not maintain a cause of action against a professional for his negligence in structuring an investment or in rendering an opinion to a client upon which the investor relied. This rule was
announced in Ultramares Corp. v. Touche.90

Courts have since steadily eroded the rule announced in Ultramares and some have actually erased its influence in certain well-defined situations.91 The modern trend holds that an action by a third party will lie against an attorney where the performance of the latter's services are intended to affect the third party, the harm is foreseeable, a close connection exists between the attorney’s conduct and the harm suffered, the blame is on the attorney, and the policy of the jurisdiction is to prevent future harm of a similar nature.92 Often these cases involve the issuance of opinion letters by attorneys.93 Thus, the established trend

90 255 N.Y. 170, 174 N.E. 441 (1931). In Ultramares, a firm of accountants negligently prepared a report on its client’s financial status showing the company to be in sound financial condition when in fact it was insolvent. Id. at 175, 174 N.E. at 442. Although the accountants knew that the report would be shown by the company in the ordinary course of its business to banks, creditors, shareholders, and other third parties, it did not know the frequency with which it would be used nor to whom it would be shown. Id., 174 N.E. at 442. Relying on the report, the plaintiff loaned money to the company and shortly thereafter the company was declared bankrupt. Id., 174 N.E. at 442. The plaintiff who was injured as a result of the company’s insolvency sued the accountants for negligence and fraud. Id., 174 N.E. at 442. The court dismissed the cause of action for negligence, concluding that the accountants did not owe a duty of care to third party, non-client investors:

If liability for negligence exists, a thoughtless slip or blunder, the failure to detect a theft or forgery beneath the cover of deceptive entries, may expose accountants to a liability in an indeterminate amount for an indeterminate time to an indeterminate class. The hazards of a business conducted on these terms are so extreme as to enkindle doubt whether a flaw may not exist in the implication of a duty that exposes to these consequences.

Id. at 179, 174 N.E. at 444.


92 See Donald v. Garry, 19 Cal. App. 3d 769, 97 Cal. Rptr. 191 (1971) (attorney representing a collection agency held liable to a creditor whose action was dismissed because of the attorney’s failure to diligently prosecute the agency’s claim); Lucas v. Hamm, 56 Cal. 2d 583, 364 P.2d 685, 15 Cal. Rptr. 821 (1961) (attorney owed a duty of care to beneficiaries of a will which failed because the will, as drafted, violated the rule against perpetuities); accord Biankaja v. Irving, 49 Cal. 2d 647, 320 P.2d 16 (1958); Guy v. Liederbach, 279 Pa. Super. 543, 421 A.2d 333 (1980).

93 See, e.g., Roberts v. Ball, Hunt, Hart, Brown & Baerwitz, 57 Cal. App. 3d 104, 128 Cal. Rptr. 801 (1976) (attorney held liable to a third party lender for his incorrect opinion of a partnership’s status where the opinion was rendered for the purpose of influencing the lender); Goodman v. Kennedy, 18 Cal. 3d 335, 556 P.2d 737, 134 Cal. Rptr. 375 (1976) (attorney not liable to a purchaser of stock where the purchaser was not the intended beneficiary of the attorney’s negligent advice to the seller); accord United Leasing Corp. v. Miller, 263 S.E.2d 313 (N.C. App. 1980).

In Reamer v. Kessler, 233 Md. 311, 196 A.2d 896 (1964), an attorney was held liable to third party lenders where he was retained to organize two corporations and to seek loans for them to be secured by construction equipment which the client was to transfer to the corporations. In each instance, the lenders received a certificate from the attorney that the borrowing corporation had good title to the equipment which was being used as security for the two loans. The attorney in issuing the certificates merely relied upon his client’s representation that he had good title. He did not make an independent investigation. Had
firmly supports an attorney's direct liability to investors for his negligent preparation of a tax shelter opinion.

2. Revised 346 Creates a Duty of Care to Investors

Revised 346 explicitly recognizes that an attorney's role in preparing a tax shelter opinion is that of an advisor and it clearly implies that an attorney who fails to exercise reasonable care in the performance of this task should be liable to third party investors:

The Proposed Model Rules specifically recognize the ethical considerations applicable where a lawyer undertakes an evaluation for the use of third persons other than a client. These third persons have an interest in the integrity of the evaluation. The legal duty of the lawyer therefore "goes beyond the obligations a lawyer normally has to third persons." 

Revised 346 repeatedly emphasizes the necessity of protecting investors. Indeed, the existence of third party reliance defines the tax shelters to which Revised 346 applies. A "tax shelter opinion" (for purposes of Revised 346) is that which is "directed to persons other than the client who engage[d] the lawyer to . . . give advice. . . [T]he term does not . . . include rendering services solely to the offeror."

Thus, by its own terms, Revised 346 imposes a duty of care on

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94 The lawyer rendering a tax shelter opinion which he knows will be relied upon by third persons, however, functions more as an advisor than as an advocate . . . . Because third persons may rely on the advice of the lawyer who gives a tax shelter opinion, the principles announced in A.B.A. Formal Opinion 314 have little, if any, application. Revised 346, supra note 4, at 4. See also text accompanying notes 174-81 infra.

95 Revised 346, supra note 4, at 4 (citing MODEL RULES OF PROFESSIONAL CONDUCT Rule 2.3 at 117 (ABA Comm'n on Evaluation of Professional Standards, Proposed Final Draft, May 30, 1981)).

96 See, e.g., Revised 346, supra note 4, at 1:

The promoter of the offering may depend upon the recommendations of the lawyer in structuring the venture and often publishes the opinion with the offering materials or uses the lawyer's name in connection with sales promotion efforts. The offerees may be expected to rely upon the tax shelter opinion in determining whether to invest in the venture. It is often uneconomic for the individual offeree to pay for a separate tax analysis of the offering because of the relatively small sum each offeree may invest.

97 Revised 346, supra note 4, at 2 (emphasis added). However, advice to an offeror does constitute a "tax shelter opinion" if the name of the lawyer or the fact that a lawyer has rendered an opinion is mentioned in the offering materials or in the sales promotion efforts. Id. See also note 53 supra.
attorneys in favor of investors. Nevertheless, this does not mean that courts will recognize Revised 346 as authority in legal malpractice cases between an attorney and such an investor. Although no court has specifically addressed the issue, we can draw some conclusions by examining the treatment accorded other rules of ethics in imposing legal duties on attorneys.

3. Use of Ethics to Define Those to Whom Attorneys Owe a Duty of Care

Although many courts have consistently rejected the use of ethics in defining the scope of legal duties which attorneys owe to non-clients, these cases appear to be mere affirmations of the long established rule that an attorney does not owe a duty of care to an adverse party, rather than a rejection of third party liability itself. A careful review of these cases suggests that instead of re-

98 "[T]he lawyer who issues a tax shelter opinion should follow . . . the Ethical Considerations of the Model Code." Revised 346, supra note 4, at 3. Revised 346 also points out that the Model Rules impose a duty in favor of tax shelter investors on an attorney making an evaluation. Id. at 4. Third persons have an interest in the integrity of the evaluation. MODEL RULES OF PROFESSIONAL CONDUCT, supra note 95, at 117.

99 See, e.g., Martin v. Trevino, 578 S.W.2d 763, 770 (Tex. Civ. App. 1978) (court rejected use of ethical standards "[r]egardless of the merit[s] of such [a] contention"). In Bickel v. Mackie, 447 F. Supp. 1376 (N.D. Iowa 1978), aff'd, 590 F.2d 341 (8th Cir. 1983), an attorney brought an unsuccessful medical malpractice action against a physician. The physician then sued the attorney for malicious prosecution, abuse of process, negligent practice of law, failure to comply with the Code of Professional Responsibility, and conspiracy. The court rejected the physician's argument that a violation of the Code of Professional Responsibility, like a violation of a statute, constitutes negligence per se. 447 F. Supp. at 1383. In so holding, the court stated:

Violation of the Code of Professional Ethics is not tantamount to a tortious act, particularly with regard to liability to a non-client. Though Canon 7 does speak of a duty "to the legal system" to stay within the bounds of the law when representing clients, it does not create a private cause of action.


100 In Ayyildiz v. Kidd, 220 Va. 1080, 266 S.E.2d 108 (1980), the court, citing Brody v. Ruby, supra note 99, noted that:

In other states inroads have been made in the privity doctrine as it pertains to legal malpractice, but where these inroads have occurred, the third party has been a direct and intended beneficiary of the lawyer's services. An adverse party does not stand in this position.

Id. at 1086, 266 S.E.2d at 113 (emphasis added). On the other hand, the Model Rules of Professional Conduct (MRPC) contain a disclaimer which discourages use of the MRPC as a reference for defining legal duties in civil litigation:

The fact that a Rule is a just basis for a lawyer's self-assessment, or for sanctioning a lawyer under the administration of a disciplinary authority, does not imply that an antagonist in a collateral proceeding or transaction has standing to seek enforcement of the Rule. Accordingly, nothing in the rules should be deemed to augment any substantial legal duty of lawyers or extra disciplinary consequences of violating such a duty.

MODEL RULES OF PROFESSIONAL CONDUCT Preamble (1980) (emphasis added). If adverse
jecting the theory, courts will hold that ethical standards may define
the legal duties that an attorney owes to nonadverse third parties.

In Nelson v. Miller, a physician, who had prevailed in a med-
cal malpractice action, sued his former adversaries’ attorneys for
malicious prosecution and negligence. He sought to establish lia-


ability based upon violations of disciplinary rules prohibiting the fil-
ing of frivolous lawsuits and those designed merely to harass or
maliciously injure another. The court rejected the argument that
a breach of those rules gave rise to a cause of action against an
adversary attorney. However, the court recognized that a cause
of action normally does exist for non-clients in situations involving
foreseeable injury to third party beneficiaries of an attorney’s serv-
ices. This is precisely the situation which exists when an attorney
issues tax shelter opinions for the benefit of prospective investors.
Moreover, the Nelson court would probably consider Revised 346 in
evaluating the standards within the profession.

In a factually similar case, Brody v. Rudy, the Iowa Supreme
Court rejected the same argument proposed in Nelson v. Miller. But
in doing so, the court made clear that its decision rested on the
critical fact that the third party was the attorney’s adversary:

The [lawyer has an] obligation to represent his or her client
zealously within the bounds of the law. . . . The basic adversary
nature of the legal profession . . . must be accompanied by im-
munity from liability for negligence in an action by a successful
adverse litigant.

We hold the Iowa Code of Professional Responsibility fur-
nishes no basis for a private cause of action for negligence in the
circumstances of this case.

The Brody court, citing Ryan v. Kanne, held that “in order

party is substituted for antagonist, the MRPC’s disclaimer merely states the general rule.
Moreover, although the MRPC discourages its use in civil litigation, the MRPC contains a
different direction regarding third party beneficiaries:

An evaluation may be performed at the client’s direction but for the primary
. . . benefit of third parties; for example, an opinion . . . rendered at the behest of
a vendor for the information of a prospective purchaser . . . .

... .

When the evaluation is intended for the use of a third person, a legal duty to that person
may or may not arise. That legal question is beyond the scope of this rule. However,
since such an evaluation involves a departure from the normal client-lawyer rela-
tionship, careful analysis of the situation is required.

Id. at Rule 2.3 comment (evaluation for use by third persons) (emphasis added).

102 Id. at 286, 607 P.2d at 450.
103 Id. at 289, 607 P.2d at 451.
104 Id. at 287, 607 P.2d at 450.
105 See text accompanying note 83 supra.
106 267 N.W.2d 902 (Iowa 1978).
107 Id. at 907 (emphasis added).
108 170 N.W.2d 395 (Iowa 1969). In Ryan the court held that accountants could be lia-
[for a third person] to proceed successfully in a legal malpractice action, [he] must be a direct and intended beneficiary of the lawyer’s services.” 109 A tax shelter investor is just such “a direct and intended beneficiary of the lawyer’s services.”

These cases reveal that, in appropriate circumstances, courts will apply ethical standards to define those persons to whom an attorney owes a duty of care. This should be particularly true where an application of those standards would yield results consistent with common law. Such a situation existed in *Egan v. McNamara*. 110 In the *Egan* case, a shareholder entered into a buy-sell agreement with his corporation and other shareholders, including the corporation’s attorney. 111 The agreement provided that the corporation would purchase all the common stock of each shareholder upon his death in accordance with a stated formula. 112 The shareholder died and the corporation purchased his shares as provided by the agreement. However, the executor of the shareholder’s estate was unsatisfied with the results, and sued to rescind the agreement on the grounds that the corporation’s attorney had breached a fiduciary duty owed to the shareholder. 113 The court rejected the argument because an analysis of the jurisdiction’s code of ethics revealed that, as a representative of the corporation, the attorney owed a duty only to that entity and not to the shareholder. 114 Moreover, the “result under the Code [of Ethics was] wholly consistent with relevant case law.” 115

Although there is admittedly little authority on point, the theory that rules of ethics may define those to whom an attorney owes a duty of care is sound. Clearly, Revised 346 attempts to impose such a duty on attorneys for the benefit of tax shelter investors. Moreover, this result is entirely consistent with the

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109 267 N.W.2d at 906.
111 Id. at 737.
112 Id.
113 Id. at 737-38. The executor argued that the duty running from the corporation’s attorney to the shareholder was based either upon an attorney-client relationship or upon a relationship of trust between two stockholders in a close corporation. Id. at 738.
114 Id. at 738.
115 Id. at 739. The court was referring to *Fielding v. Brebbia*, 479 F.2d 195 (D.C. Cir. 1973). The court there held that “[t]he corporation is the client . . . [and] business confidences of business partners lack the protection of professional privilege.” Id. at 198. The *Egan* court went on to analogize to the *Fielding* facts by noting that in *Egan* the attorney did not receive separate compensation for the legal services rendered to the shareholder and that the services had no bearing upon the agreement. 467 A.2d at 739. The court concluded that *Fielding* did not err by rejecting the suggestion of an attorney-client relationship. Id.
developing trend in case law. \textsuperscript{116} Therefore, at least in the tax shelter area, an attorney's liability to investors should prove indisputable.

C. Use of Ethics to Define the Standard of Care in Legal Malpractice Actions

Even if courts reject the independent authority of Revised 346 to establish that tax shelter attorneys have legal duties for malpractice which accrue to tax shelter investors, Revised 346 will still serve as compelling support for the conclusion that such a duty should exist under common law. \textsuperscript{117}

Although the Model Rules of Professional Conduct "simply provide a framework for the ethical practice of law," \textsuperscript{118} many have accepted the persuasive argument that courts should use these rules more extensively. \textsuperscript{119} Unsurprisingly, courts have consistently referred to rules of ethics in formulating procedural rules \textsuperscript{120} and in cases involving disgorgement of fees, \textsuperscript{121} rescission of contract, \textsuperscript{122} and recovery of debt. \textsuperscript{123} Litigants have also used rules of ethics in criminal cases to suppress evidence, \textsuperscript{124} to request a new trial, \textsuperscript{125} and

\textsuperscript{116} See notes 100-09 supra and accompanying text.

\textsuperscript{117} The use of ethics to define the standard of care to which an attorney should be held responsible has received much more acceptance, see text accompanying notes 118-42 infra, than their use in defining those to whom an attorney owes a duty of care. This development is largely attributable to the fact that in most cases involving the latter use, adverse parties tried to use ethics to create a cause of action in their favor and courts have steadfastly refused to extend an attorney's liability to them. See notes 100-09 supra and accompanying text. Also, as in Egan v. McNamara, 467 A.2d 735 (D.C. 1983), resort to rules of ethics to define those to whom an attorney owes a duty of care would in most instances produce the same results as an analysis of the common law. Therefore, reference to rules of ethics in these cases, although helpful, may be unnecessary.

\textsuperscript{118} MODEL RULES OF PROFESSIONAL CONDUCT, supra note 100, at Preamble.


\textsuperscript{121} In re Eastern Super Litigation, 697 F.2d 524 (3d Cir. 1982); Financial General Bankshares, Inc. v. Metzger, 523 F. Supp. 744 (D.D.C. 1981) (breach of ethical rules required disgorgement of fees), vacated, 680 F.2d 768 (D.C. Cir. 1982). But see Delano v. Kitch, 663 F.2d 990, 998 n.9 (10th Cir. 1981) (declined to "inject issue of whether the Code [of Professional Responsibility] should serve as the basis for private litigation into this action"). See also Knighten v. Knighten, 447 So. 2d 534, 543 (La. App. 1984) (ethical standards used to measure the reasonableness of a fee).


\textsuperscript{124} See, e.g., United States v. Jamil, 546 F. Supp. 646 (E.D.N.Y. 1982), rev'd, 707 F.2d 638, 645-46 (2d Cir. 1983) (court accepted argument that violations of ethics can justify suppression of evidence but found that no violations had occurred).

\textsuperscript{125} State v. Dean, 67 Wis. 2d 513, 227 N.W.2d 712 (1975).
to assert ineffective assistance of counsel.126 Furthermore, courts have applied these rules extensively in disqualifying opposing counsel,127 notwithstanding an express code prohibition against their use as a “procedural weapon” against adversaries.128 Incredibly, one jurisdiction has gone so far as to apply the lawyer’s code of ethics to dentists in a dental malpractice action.129

The most extensive use of rules of ethics occurs in actions for breach of fiduciary duty and legal malpractice.130 Courts follow this course despite the Code’s disclaimer131 that it is not intended to be used in civil litigation132 and, in some cases, the active opposition to its use by the bar.133 Some courts, however, have accepted the Code’s disclaimer as dispositive.134 But more courts have not

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126 Summers v. Thompson, 444 F. Supp. 312 (M.D. Tenn. 1977). See also Gaudineer, supra note 10, at 102-06.
128 MODEL RULES OF PROFESSIONAL CONDUCT, supra note 100, at Preamble. See also note 100 supra.
129 Porubiansky v. Emory University, 156 Ga. App. 602, 610 n.2, 275 S.E.2d 163, 169 n.2 (1980) (court found exculpatory clause void as against public policy noting that the state code of ethics prohibited attorneys from limiting their liability to clients, stating: “We see no reason why other professionals, such as dentists, should not be held to a similar standard.”), aff’d, 248 Ga. 391, 282 S.E.2d 903 (1981).
131 See notes 100 and 128 supra and accompanying text.
132 "We recognize that the Code of Professional Responsibility 'does not undertake to define standards for civil liability of lawyers for professional conduct' . . . . Nevertheless, it certainly constitutes some evidence of the standards required of attorneys." Woodruff v. Tomlin, 616 F.2d 924, 936 (6th Cir.), cert. denied, 449 U.S. 888 (1980).
133 See, e.g., Rogers v. Robson, Masters, Ryan, Brumund & Belom, 81 Ill. 2d 201, 407 N.E.2d 47 (1980) (court found attorney liable for failure to disclose to his client the intent to settle). The Illinois Defense Counsel and Illinois State Bar Association participated in the case as amici curiae urging that “the appellate court erred in implying that proof of a violation of the canons or disciplinary rules of the American Bar Association Code of Professional Responsibility established a per se basis for imposing liability on an attorney in a malpractice action.” Id. at 204, 407 N.E.2d at 48.
134 See, e.g., Greening v. Klamen, 652 S.W.2d 730, 734 (Mo. App. 1983).
found the disclaimer compelling. This is undoubtedly because the Code clearly enunciates the conduct expected of attorneys and because much of its language sounds in negligence. As such, it is a well-articulated reference point, too irresistible to ignore. Furthermore, these courts recognize the common sense notion that because "[e]very lawyer is responsible for observance of [these] rules," they are designed to protect the public interest. Thus, there is no good reason why the rules should not also provide the basic evaluation tools for courts which judge the quality of an attorney's performance.

Consider the reasoning of the court in Lipton v. Boesky. In rejecting a defendant attorney's argument that his alleged breach of several disciplinary rules was not actionable, the court stated:

The Code of Professional Responsibility is a standard of practice for attorneys which expresses in general terms the standards of professional conduct expected of lawyers in their relationships with the public, the legal system, and the legal profession. Holding a specific client unable to rely on the same standards in his professional relations with his own attorney would be patently unfair. We hold that, as with statutes, a violation of the Code is rebuttable evidence of malpractice.

This reasoning is compelling.

While some courts have avoided ruling on the issue, others have gone so far as to hold that a plaintiff's complaint in a legal malpractice action failed to state a claim upon which relief could be granted where the complaint failed to allege all matters necessary to constitute a breach of a disciplinary rule.

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135 See notes 130 and 132 supra.
136 See, e.g., MODEL RULES OF PROFESSIONAL CONDUCT, supra note 100, at Rule 1.1 (competence).
137 Id. at Preamble.
139 Id. at 597-98, 313 N.W.2d at 166-67 (citation omitted).
140 Saul v. Blumenfeld, 445 A.2d 613 (D.C. 1982) (court in a legal malpractice action failed to rule on appellant's claim that the trial court erred in refusing to allow evidence based upon the Code of Professional Responsibility). In Johnson v. Jones, 103 Idaho 702, 652 P.2d 650 (1982), the court stated:

The more difficult question is whether a cause of action for legal malpractice ... [may arise from] the failure of [an] attorney [in] fulfill[ing] fiduciary responsibilities imposed by the Code of Professional Conduct. Without foreclosing the possibility that such a cause of action might be maintained in some circumstances, we hold that the breach ... alleged in this case did not serve as the basis for an action for legal malpractice.

141 See, e.g., Chicago Title Ins. Co. v. Holt, 36 N.C. App. 284, 288, 244 S.E.2d 177, 182 (1978) (complaint that attorney improperly represented multiple parties failed to state a valid claim where it was not alleged that the attorney failed to disclose his multiple representation as required by the state code of ethics).
The use of Revised 346 in tax shelter malpractice cases will merely reflect this well-reasoned application of ethics in defining an attorney's duty of care in general legal malpractice actions. Courts which have accepted the general principle have not only referred to disciplinary rules and ethical considerations within the Code, they also have utilized formal ethics opinions of the ABA and of their respective state bar organizations. Thus, there is sufficient authority to warrant reference to Revised 346 for guidance in determining the standards required of attorneys in legal malpractice cases involving failed tax shelters.

IV. Ramifications of the Application of Revised 346

A. Proof of Applicable Ethical Standards

Ordinarily, in legal malpractice actions, plaintiffs must use expert witnesses to testify as to the degree of care and skill demanded in the particular situation. An exception to this rule exists where the alleged negligence of the attorney is so obvious that it is within the range of experience and understanding of nonprofessionals. But where the case involves the attorney's failure to observe accepted standards in issuing a tax shelter opinion, this exception does not apply. Here, in order to establish a prima facie case of malpractice, the plaintiff must provide expert testimony by an attorney who has knowledge of tax shelter practice and the ethical standards which apply.

The presence of legal ethics experts in the courtroom has increased as courts grow more receptive to the use of the rules of ethics as evidence of the applicable standard of care for attorneys. Such acceptance involves close scrutiny of the expert's testimony. Thus, in Kirsch v. Duryea, for example, where the plaintiff's expert testified that the defendant-attorney was negligent

143 D. MEISELMAN, supra note 84, at 149-55.
145 See D. MEISELMAN, supra note 84, at 153-54.
146 See Kirsch v. Duryea, 21 Cal. 3d 303, 578 P.2d 935, 146 Cal. Rptr. 218 (1978) (court expressly rejected ethics expert's testimony as it was inconsistent with the ABA and state bar rules of ethics); DiPiero v. Goodman, 14 Mass. App. 929, 436 N.E.2d 998 (1982) (expert's testimony of breach of ethics if properly formulated would have been sufficient in law to support a finding of malpractice). See also Raine v. Drasin, 621 S.W.2d 895 (Ky. 1981) (malicious prosecution and abuse of process actions in which a deposition of a law professor and member of the Ethics Committee of the Louisville Bar Association was read to the jury).
147 21 Cal. 3d 303, 578 P.2d 935, 146 Cal. Rptr. 218 (1978).
in not seeking an immediate, nonconsensual withdrawal (when he concluded that the plaintiff's original case lacked merit), the California Supreme Court rejected such testimony because it was contrary to the ABA's disciplinary rules (which required the attorney to take all reasonable steps to avoid prejudicing his client's rights prior to withdrawal).\textsuperscript{148}

Similar reasoning, in the context of a legal malpractice action arising out of the issuance of a tax shelter opinion, could lead a court to reject an expert's opinion as to the standard of care to be applied in a particular case if it is inconsistent with the requirements of Revised 346. In fact, courts may have to instruct the jury to choose between experts. In cases of this nature, experts will refer to Revised 346 and opine that the defendant-attorney did (or did not) comply with its terms (depending on whose behalf the expert testifies). Such conflicting testimony should raise interesting questions of mixed law and fact. However, the more interesting area of development will be the extent to which these experts do disagree—their debate on what Revised 346 actually requires and how it applies to different factual scenarios. Given the nature of an expert's role in malpractice actions, disagreement itself appears to be a certainty.

**B. Impact of Revised 346 on Custom**

Evidence of the customary practice in a community is generally admissible on the question of what standard applies in a legal malpractice action.\textsuperscript{149} This rule is consistent with the general principles of tort law which measure the conduct of an actor against that of the other members of his community.\textsuperscript{150} "Considerations of fairness, a judicial desire to further efficiency by encouraging adherence to readily observable standards, and an instinct to defer to the general demonstrated proclivities of the group have uniformly persuaded courts to admit evidence of custom and habit as bearing on the question of due care."\textsuperscript{151}

However, as demonstrated by *Gleason v. Title Guarantee Co.*,\textsuperscript{152} evidence of compliance with customary practice does not guarantee insulation from liability in a legal malpractice action. In *Gleason*, an attorney, retained to examine title to real estate and to verify that the desired mortgages would not be subordinate to existing mort-

\begin{itemize}
\item \textsuperscript{148} Id. at 311, 578 P.2d at 940, 146 Cal. Rptr. at 223. See Model Code of Professional Responsibility DR 2-111(A)(2) (1977).
\item \textsuperscript{149} R. MALLEN & V. LEVIT, supra note 1, at 338-40.
\item \textsuperscript{150} Wolfram, supra note 10, at 294; see note 83 supra and accompanying text.
\item \textsuperscript{151} Wolfram, supra note 10, at 294.
\item \textsuperscript{152} 300 F.2d 813 (5th Cir. 1962), reh'g denied, 317 F.2d 56 (5th Cir. 1963). See also note 1 supra and accompanying text.
\end{itemize}
gages,\textsuperscript{153} represented that he had personally reviewed the relevant records.\textsuperscript{154} Actually, he had merely relied upon incorrect information provided to him over the telephone by an abstract company.\textsuperscript{155} When his client sued him for legal malpractice, the attorney defended his conduct on the ground that it was customary for attorneys in his community to make title certifications in that manner.\textsuperscript{156} The court rejected his argument, holding that:

While custom provides an important indication of what constitutes reasonable care and what is negligent, it is not dispositive of the question at issue. All customs are not good customs, and lawyers have no prescriptive right to make knowingly false statements in the name of custom. . . . We can sympathize with the defendant in the fact that he is to be heavily penalized for following the custom while others, perhaps even those who established the custom, may escape adverse consequences. Nevertheless, the custom was improper, and its existence cannot alter [the attorney's] responsibility . . . .\textsuperscript{157}

Thus, compliance with customary practice is not dispositive.\textsuperscript{158} While custom may help define the applicable standard of care, it will not insulate an attorney from liability if a reasonable person would not follow the custom.\textsuperscript{159}

Thus, an attorney charged with failing to follow Revised 346 ordinarily could not successfully contend that his conduct was reasonable and not actionable solely because it was in conformance with the customary practice, the very practice condemned in Revised 346. Instead the attorney would also have to show that, \textit{given the requirements of Revised 346}, the custom still states the standards which a reasonable person would follow.

This result is not unfair. The terms of Revised 346 are not unduly burdensome or unreasonable. Furthermore, extensive discussion of the need to correct unacceptable practices in this area\textsuperscript{160} places attorneys on notice that the government, the bar, and the public have grown impatient with them; that those who ignore Revised 346 are unnecessarily exposing themselves to liability, and that they are, therefore, undeserving of sympathy.\textsuperscript{161}

\textsuperscript{153} 300 F.2d at 814.
\textsuperscript{154} Id.
\textsuperscript{155} Id.
\textsuperscript{156} Id.
\textsuperscript{157} Id. (citations omitted). \textit{See also} text accompanying note 1 supra.
\textsuperscript{158} \textit{See generally} 7A C.J.S. Attorney-Client \textsection{} 254 (1980).
\textsuperscript{159} R. MALLEN \& V. LEVIT, supra note 1, at 338-40; \textit{see} text accompanying notes 1-5 supra.
\textsuperscript{160} See the collection of articles cited in Special Comm. on the Lawyer's Role in Tax Practice, Ass'n of the Bar of the City of New York, \textit{Tax Lawyer's Role in Tax Practice}, 36 Tax Law. 865, 872 n.31 (1983).
\textsuperscript{161} \textit{See}, e.g., Kuehn v. Garcia, 608 F.2d 1143, 1146 (8th Cir. 1979) (attorney found in
C. Causation

In any legal malpractice action the plaintiff must show that the attorney's negligent act or omission was the proximate cause of his damages. In the case of an investor in a failed tax shelter, this would typically mean that the investor would have to show that he received the tax shelter opinion, that he read it, that he relied on it in investing in the shelter, and that the attorney's advice or lack thereof caused his damages. Since investors commonly rely upon tax shelter opinions, causation should not present an insurmountable barrier to recovery of damages.

D. Damages

Tax shelter malpractice cases present no unique damages issues. Damages issues in these cases will usually be resolved by each jurisdiction's normal civil rules. Typically, tax malpractice damages include attorney's fees, and amounts equal to the assessed penalties and interest. Additionally, the attorney should compensate the investor for the loss of tax benefits which the investor reasonably expected to derive from the investment. 

breach of ethical rules at a disciplinary hearing may be barred from relitigating his liability to an investor in a subsequent malpractice suit by collateral estoppel).  

162 See D. MEISELMAN, supra note 84, at 40-43. See also text accompanying note 84 supra.  
163 Many commentators share the view expressed in the Report of the Executive Committee of the Tax Section, New York State Bar Association Tax Section, supra note 2, at 203: An indeterminate number of investors in tax shelters are ignorant of the subtleties involved and are unable to evaluate the complexities of the legal discussion [in the tax shelter opinion]—if, indeed, they even read it. Many of them probably take the mere presence of the lawyer's opinion as an indication that the desired tax benefits will be achieved (even if the opinion is more guarded than that). Other investors know full well that the shelter is subject to serious question, but assume that the lawyer's opinion means that the transaction—at least as to the investor—provides a possible reporting position that may prevail if audited.  

164 R. MALLEN & V. LEVIT, supra note 1, at 349.  
166 Some may think that awarding expectation damages is unwarranted in tax shelter cases, especially where the plaintiff invested in an abusive tax shelter. However, a careful analysis reveals that such damages are justifiable. If the attorney issued a favorable opinion when a negative opinion was warranted, the investor would have refrained from investing in this tax shelter; he would, nonetheless, have invested in another which would have, or at least could have, provided the benefits expected from the first. Thus, since the attorney was negligent in his appraisal of the first, the investor lost the opportunity and the benefits which the opportunity entailed.  

On the other hand, if the attorney issued a negative opinion instead of a favorable one, unless the investor refrained from investing in any tax shelter, he should not recover any expectation damages, or at least none greater than the difference between the first (assuming its benefits were greater) and the one in which he actually invested.  

For a thorough analysis of the damages recoverable in legal malpractice cases involving
Generally, courts do not award punitive damages in legal malpractice cases in the absence of fraud, malice, or oppression. \footnote{1}{167} However, fraud does exist in cases where an attorney makes statements with reckless or conscious disregard of the truth. \footnote{168} Some jurisdictions even permit punitive damages where there is simply "gross negligence." \footnote{169} Thus, investors \textit{should} recover punitive damages against an attorney where the attorney's conduct is an egregious violation of the disciplinary standards contained in Revised 346, and \textit{may} recover them for less oppressive conduct.

Revised 346 provides that an attorney issues a false opinion whenever he "accepts as true the facts the [offeror-client] . . . tells him, when . . . [he] should know that a further inquiry would disclose . . . [those] facts as untrue." \footnote{170} Furthermore, an attorney who renders a false opinion \footnote{171} is guilty of "conduct involving dishonesty, fraud, deceit, or misrepresentation" in violation of disciplinary rules. \footnote{172} Clearly, in these cases it is difficult to dispute the appropriateness of punitive damages.

\section*{E. Use of Ethical Rules as a Defense}

Ethical standards have mostly aided plaintiffs who have argued that a breach of the rules of ethics constitutes legal malpractice. However, courts have also accepted evidence of compliance with the rules as evidence of conformance to the applicable standards of due care. \footnote{173} Sometimes both sides in a legal malpractice action have made a case based on the rules of ethics.

\textit{Hawkins v. King County} \footnote{174} provides a final example of the potential uses of ethical standards. In the \textit{Hawkins} case, the plaintiff advised his court-appointed defense attorney that he wished to be released on bail pending the disposition of criminal charges against him. \footnote{175} Prior to the bail hearing, the attorney learned that the plaintiff was mentally ill and dangerous to others. This information

\begin{footnotesize}
\footnote{167}{Stinson v. Feminist Women's Health Center, 416 So. 2d 1183, 1185 (Fla. App. 1982).}
\footnote{168}{Welder v. Mercer, 247 Ark. 999, 448 S.W.2d 952 (1972).}
\footnote{170}{Revised 346, \textit{supra} note 4, at 3.}
\footnote{171}{See note 37 \textit{supra}.}
\footnote{172}{Revised 346, \textit{supra} note 4, at 3.}
\footnote{174}{24 Wash. App. 338, 602 P.2d 361 (1979).}
\footnote{175}{Id. at 340, 602 P.2d at 363.}
\end{footnotesize}
came from a psychiatrist who had examined the plaintiff and from another attorney who had been hired by the plaintiff's mother to assist in having the plaintiff hospitalized or civilly committed.\textsuperscript{176}

At the bail hearing, the attorney did not offer the information and no questions were directed to him in this vein. The plaintiff was released.\textsuperscript{177} Eight days later, the plaintiff assaulted his mother and attempted suicide by jumping off a bridge. This attempt at self-destruction resulted in injuries requiring the amputation of both of his legs.\textsuperscript{178}

The plaintiff sued the attorney for legal malpractice for failing to reveal his mental condition to the court in contravention of both the court's rules and the ethical rule that "a lawyer shall not . . . [i]n his representation of a client . . . [c]onceal or knowingly fail to disclose that which he is required by law to reveal."\textsuperscript{179} The court rejected the plaintiff's claim, finding that the attorney did not have to disclose this information and that the attorney's conduct was proper because of his duty of loyalty and his ethical duty to "advocate zealously his client's interests" as required by the Code.\textsuperscript{180} Significantly, the tax shelter attorney is not an advocate,\textsuperscript{181} and, therefore, he should not be able to make the same defense.

V. Conclusion

The use of ethics to measure an attorney's liability for legal malpractice is a developing but well-entrenched practice. Revised 346 is the single most authoritative statement on accepted professional standards in the area of tax shelter opinions. Therefore, courts will inevitably resort to Revised 346. Although some courts may reject the argument that Revised 346 sets the definitive standard, or that it constitutes evidence of the standard of care in this area, it is likely that attorneys will nevertheless adhere to Revised 346's guidelines either voluntarily or because they will fear its potential use in legal malpractice actions. Consequently, the guidelines of Revised 346 should eventually evolve into customary practice, and, therefore, ultimately set the standards for measuring an attorney's performance in rendering a tax shelter opinion.

Tax shelter attorneys stand forewarned. The mere existence of Revised 346 has alerted the tax bar to particular problems, such as overvaluation, in the tax shelter area. Accordingly, those who fail

\textsuperscript{176} Id.
\textsuperscript{177} Id.
\textsuperscript{178} Id.
\textsuperscript{179} Id. at 342, 602 P.2d at 363 (citing MODEL CODE OF PROFESSIONAL RESPONSIBILITY DR 7-102(A)(3) (1976)).
\textsuperscript{180} 24 Wash. App. at 343, 602 P.2d at 364.
\textsuperscript{181} See note 94 supra and accompanying text.
to exercise extra caution in the areas which Revised 346 addresses cannot complain when courts apply its standards to find them liable for abusive tax shelter opinions. Such an attorney is manifestly at fault.