



Securities Industry Association

120 Broadway, New York, NY 10271-0080, (212) 608-1500, Fax (212) 608-1604
1401 Eye Street, NW, Washington, DC 20005-2225, (202) 296-9410, Fax (202) 296-9775
info@sia.com, <http://www.sia.com>

October 22, 2002

Giovanni Prezioso, General Counsel
Meyer Eisenberg, Deputy General Counsel
U.S. Securities and Exchange Commission
450 Fifth Street, NW
Washington, DC 20549

Dear Mr. Prezioso and Mr. Eisenberg:

The Securities Industry Association ad hoc committee on Section 307 of the Sarbanes-Oxley Act ("Committee") submits this preliminary expression of views in the hopes of assisting the Commission and its staff in formulating rules under Section 307 of the Sarbanes-Oxley Act.¹ That provision requires the Commission to promulgate rules setting forth minimum standards of professional responsibility for attorneys "practicing before the Commission in any way in the representation of issuers" In particular, Section 307 requires the Commission to promulgate a rule requiring attorneys who come across evidence of misconduct within an issuer to report that evidence to the chief legal officer or chief executive officer of the organization. If that person fails to take "appropriate remedial action," the attorney must then report the evidence to a higher authority within the organization. That higher authority may be either the audit committee, the board of directors, or a committee made up of non-employee board members.

The Committee understands that this "up-the-ladder" reporting requirement is designed to serve the public interest and may prove to be an important tool in protecting investors and in preventing fraud by issuers. In promulgating rules under Section 307, the Commission undoubtedly will consider the ambiguities in the statutory language. In addition, the Commission will have considerable discretion in determining how to exercise its authority in the public interest and in the interest of investors.

SIA brings together the shared interests of more than 600 securities firms to accomplish common goals. Its member firms (including investment banks, broker-dealers, and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. SIA therefore has a substantial interest in the Commission's upcoming rulemaking. The securities industry is heavily regulated and employs thousands of attorneys to assist member firms in fulfilling their legal obligations under the federal securities laws. Because the federal securities laws pervade the securities industry, and because of the high reliance the industry has

¹ Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (2002).

on the attorneys that assist it, SIA member firms have a major stake in the Commission's rulemaking in this area.

While we cannot anticipate all issues the Commission intends to cover in its upcoming proposals, and as to which we may want to comment, we hope that the following points might be useful to the Commission in considering what to propose. In brief, the SIA urges the Commission to:

- Delineate clearly the class of persons subject to Commission rules of professional responsibility for attorneys;
- Specify that an attorney is obligated report evidence up the ladder only when he or she "knows" of illegal conduct;
- Adopt well-established and generally understood interpretations of materiality;
- Specify that an attorney must report violations of "fiduciary duty" or "similar violations" only to the extent those violations create disclosure or other obligations under the federal securities laws; and
- Provide clear guidelines for determining if the response by the chief legal officer or chief executive officer to a report is "appropriate."

I. The Commission Should Specify Clearly The Persons Subject To Standards of Professional Responsibility

Section 307 authorizes the Commission to promulgate rules setting forth minimum standards of professional responsibility for "attorneys appearing and practicing before the Commission in any way in the representation of issuers."² The Commission has never before defined "attorney" for purposes of its rules, and the definition of "practice before the Commission" is extremely broad. SEC Rule of Practice 102(f) defines the latter term as including "(1) transacting any business with the Commission and (2) the preparation of any statement by any attorney, accountant, engineer or other professional or expert, filed with the Commission in any registration statement, notification, application, report or other document with the consent of such attorney, accountant, engineer, or other professional."³ The definition is broad, and the Commission has traditionally interpreted it broadly, without articulating clear

² Section 602 of the Sarbanes-Oxley Act also authorizes the Commission to enforce rules of professional responsibility. It adds a new Section 4C to the Securities Exchange Act of 1934 that authorizes the Commission to deny the privilege of "appearing or practicing before the Commission" to "any person." There is substantial ambiguity as to the interplay of these provisions. In particular, there may well be a question as to whether the Commission's authority to prescribe rules with respect to "attorneys" is as broad as its authority to discipline "persons."

³ SEC Rule of Practice 102(f) at <http://www.sec.gov/about/rulesofpractice.shtml#102>.

lines between a lawyer's conduct in securities law matters that constitutes "practice" and conduct that does not.⁴

The Commission should define these terms precisely in a manner consistent with the Commission's overall responsibilities. First, the Commission should, in the opinion of the SIA, limit its definition of "attorney" to persons acting in their capacity as attorneys. Further, the definition of "appearing and practicing before the Commission" should not turn on whether the attorney's client is an entity regulated by the SEC. Also, the "up-the-ladder" reporting rule the Commission is required to promulgate pursuant to Section 307 should be limited, as the statute says, to attorneys appearing and practicing in any way before the Commission "in the representation of issuers." Finally, any such reporting duty should be limited to reports to the attorneys' clients concerning the clients' legal obligations.

A. The Commission's Attorney Rules Should Cover Only Persons Acting In Their Capacities As Attorneys.

This is a point of immense practical significance to the securities industry. Securities businesses frequently employ attorneys in non-legal positions, including investment bankers, registered representatives, human resource specialists, internal auditors, and compliance professionals. In considering its new rules, the Commission should cover only those attorneys engaged in the practice of law. The scope of the Commission's concern – and arguably the Commission's regulatory authority – should turn not merely on whether persons have the legal status as attorneys but also on whether they are acting as attorneys. Considerations of logic and fairness point to the identical result: attorneys performing the same non-legal functions should be subject to the same rules as non-attorneys performing those functions.

The legislative history of Section 307 is replete with references to the attorney's professional responsibilities to his or her client. In introducing the amendment that ultimately became Section 307, Senator Edwards emphasized that the purpose of the provision is to make sure that attorneys do their part in preventing corporate misconduct by requiring that they fulfill certain responsibilities to their ultimate clients, corporations and their shareholders, and not just to corporate management.⁵ Similarly, there are repeated statements in the legislative history by the amendment's sponsors emphasizing how the obligations of affected attorneys will be internal to the issuer, and therefore not involve a waiver of the attorney-client privilege.⁶

The attorney-client relationship is the touchstone of an attorney's professional responsibility. As the legislative history makes clear, Section 307 was intended to empower the Commission to impose rules of professional responsibility that Congress believed to be an artifact of the attorney-client relationship. The Commission has recognized that the

⁴ See, generally, Dissenting Statement of Commissioner Norman S. Johnson, Amendment to Rule 102(e) of the Commission's Rules of Practice, Release No. 33-7593 (1998) at n. 85.

⁵ 148 CONG. REC. S6551 (daily ed. July 10, 2002) (statement of Sen. Edwards).

⁶ 148 CONG. REC. S6555 (daily ed. July 10, 2002) (statement of Sen. Enzi). We do not address here the question whether an attorney's reporting obligation should arise with respect to matters outside the scope of his or her representation.

distinguishing feature of an attorney's professional activities is his obligation to work on behalf of a client.⁷

Section 307 empowers the Commission to promulgate “standards of *professional* conduct.” (Emphasis added.) What distinguishes attorneys from other employees is their “professional” relationship with the employer. That is why, for example, the applicability of the attorney-client privilege does not turn solely on whether one party to the conversation is an attorney; rather, “the lawyer must act in a legal capacity rather than perform any of the other functions of law-trained persons in our society.”⁸ While persons who are admitted to a bar may perform a wide variety of services for their employers, they should be subject to “professional” obligation only where their relationship to their employers is a professional one. It would be anomalous for the Commission to impose rules of professional responsibility on persons, even persons admitted to the bar, who except for the Commission's new rules have no professional responsibility to their employers.

Accordingly, we respectfully request that the Commission define “attorney” to mean “a person authorized to practice law and who regularly provides services pursuant to an attorney-client relationship.”

B. “Practice Before The Commission” Should Be Defined By Reference To Conduct and Not to Client.

For similar reasons, the Commission should define “practice before the Commission” with reference to conduct rather than to client. We urge the Commission to adhere to past practice and not define “practice before the Commission” so that attorneys for companies in the securities business have more exposure to liability than their counterparts working for companies in other businesses. “Appearance” and “practice” refer to conduct. We hope and expect that the Commission will not take a position that, simply because an attorney has as its client an entity that is directly regulated by the Commission, therefore all the attorney's practice constitutes “practice before the Commission.”

C. The Reporting Rule Mandated By Section 307 Applies Only To Attorneys Practicing “In The Representation Of Issuers.”

Section 307 is quite clear that whatever rules are promulgated pursuant to its authority apply only to attorneys “appearing and practicing before the Commission in any way *in the representation of issuers.*” (Emphasis added.) The phrase cannot be regarded as surplusage, particularly since it does not appear in Section 602 of the Act. Section 602 is otherwise identical with respect to its scope. Under established rules of statutory construction, the Commission

⁷ In formulating its recent auditor independence rules, the Commission distinguished between auditors and attorneys, noting that “the attorney's fundamental duty is to advance the client's interests.” See Final Rule Revision of the Commission's Auditor Independence Requirements, SEC Rel. 33-7919, 65 Fed. Reg. 76007-76090 (Dec. 5, 2000).

⁸ E.S. Epstein, *The Attorney-Client Privilege and the Work Product Doctrine* 93 (ABA Litigation Section, 3d Ed. 1997).

should give effect to differences in language in provisions in a single enactment that are otherwise the same.

D. The Reporting Requirement Rules Should Apply Only To Communications To The Attorney's Client Concerning The Client's Activities.

Although the statute does not say so explicitly, it is clear that the rule it requires would extend only to an attorney's obligation to report violations involving the attorney's client, and not third parties. The language of Section 307 nowhere suggests that attorneys must report to or about persons who are not part of their client organizations. As noted, the legislative history is focused entirely on the obligations owed by attorneys to their clients.

The point is very important to attorneys in the securities industry. The focus of their clients' work often concerns other businesses, whether in the context of investment banking, underwriting, or simply recommending the securities of various issuers. It would be an inappropriate and unreasonable burden on attorneys, and potentially chill the necessary communication of information, if the Commission were to require otherwise.

There may, of course, be instances in which the conduct of a non-client has an impact on the legal obligations of the attorney's client. To take an example, an attorney for a broker-dealer engaged in an underwriting might become aware of material mis-statements in a prospectus. This information, in turn, might well deprive the broker-dealer of a reasonable basis for recommending the security. Assuming the other requirements of Section 307 are met, the attorney for the broker-dealer might then have an obligation to report up the ladder. But the obligation, it must be emphasized, would arise as a result of the potential violation of the attorney's client, and not simply because the attorney became aware of misconduct by someone to whom the attorney owed no professional obligation.

II. An Attorney's Obligation To Report Evidence Of Violations Should Be Triggered Only When The Lawyer "Knows" Of A Violation

Section 307 does not by its terms define the specific circumstances that would trigger an attorney's obligation to report "evidence of a material violation" The natural – and, we believe, the only workable – reading is that "evidence" means only that the attorney must report the information giving rise to his or her conclusion and not merely the conclusion itself. Furthermore, the Commission should clarify that the term "evidence" connotes a triggering circumstance – i.e., that the lawyer is aware of information demonstrating the existence of a violation. The Commission should impose the obligation to report evidence of wrongdoing based on a lawyer's actual knowledge of wrongdoing, and not based on mere suspicion or conjecture.

Under existing ethical standards, an attorney must take one of a number of actions – which may or may not include reporting to senior management or a board of directors – only when a lawyer "knows" of conduct involving a violation of law. The American Bar Association Model Rule 1.13, Organization as Client, instructs an attorney to act when he or she "knows" that a person within the organization is either violating a legal obligation to the organization or

causing the organization to violate the law. Proper actions may include resignation of the representation or referring the matter to the highest authority within the company.⁹

Commission precedent is to the same effect. In the *Carter, Johnson* case,¹⁰ on which co-sponsors Senators Edwards and Corzine modeled Section 307, the SEC spoke of a lawyer's obligation to act arising when he or she "knew" that the client was engaged in illegal activity. Similarly, in the *Keating, Muething & Klekamp* case,¹¹ the Commission imposed sanctions upon a law firm with respect to a firm's failure to require disclosure of transactions with which it was involved.

As the Commission knows, the *Carter, Johnson* case provoked a firestorm of criticism, to the point that the Commission refrained from enforcing the standard it announced.¹² While the ABA's Task Force on Corporate Responsibility recently preliminarily proposed amending Rule 1.13 to require "up-the-ladder" reporting,¹³ the Task Force has yet to make a final recommendation. Accordingly, a requirement that an attorney report "up-the-ladder" when he or she "knows" of wrongdoing is a significant advance over the current state of the law.

Triggering the attorney's duty on the basis of suspicion or some other level less than knowledge would not serve the purpose of investor protection and would not work in practice. Attorneys are constantly aware of circumstances that could be consistent with, but do not demonstrate, a violation of law. Indeed, one of the principal reasons clients consult lawyers is to seek guidance when the law or the circumstances are unclear or equivocal. A "reasonable suspicion" or similar standard raises the personal stakes too much and too soon for the attorney giving advice to the client. The public interest is best served when the attorney is free to give plainspoken legal advice without undue regard for his or her self-interest. A low reporting threshold would, ironically, disserve the public by placing an excessive burden on the attorney's ability to give disinterested legal advice.

⁹ ABA/BNA LAWYERS' MANUAL ON PROFESSIONAL CONDUCT, American Bar Association and The Bureau of National Affairs, Inc. (2002), Rule 1.13(b) at 1:139.

¹⁰ In the Matter of William R. Carter, Charles J. Johnson, Jr. 1981 SEC LEXIS 1940; 47 SEC 471 (1981).

¹¹ In the Matter of Keating, Muething & Klekamp, 1979 SEC LEXIS 1186 (1979).

¹² See, e.g., *SEC's Lawyer Discipline Stance Sharply Attacked by Full ABA*, LEGAL TIMES OF WASHINGTON, Nov. 30, 1981; *ABA Files Blistering Comment on SEC Interpretation of "Unethical or Improper Professional Conduct,"* SECURITIES REGULATION & LAW REPORT, Dec. 2, 1981 at A-3. See also Edward F. Greene, Lawyer Disciplinary Proceedings before the Securities and Exchange Commission, Remarks to the New York County Lawyers' Ass'n (Jan. 18, 1982), [1981-1982 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,089. The SEC ratified Greene's speech in a 1988 release expressing the Commission's general policy of not "using its administrative forum to conduct de novo determinations of the professional obligations of attorneys." The Commission would initiate Rule 102(e) proceedings against attorneys, the release continued, only where a non-Rule 102(e) action had already found the attorney to have violated securities laws. *Disciplinary Proceedings Involving Professionals Appearing or Practicing Before the Commission*, Release No. 33-6783, 53 Fed. Reg. 26427-01, 1988 WL 278442 at 24631 (F.R.) (July 13, 1988).

¹³ Preliminary Report of the ABA Task Force on Corporate Responsibility, July 16, 2002, at <http://www.abanet.org/buslaw/corporateresponsibility/>.

The problem is not resolved by resort to some “duty to investigate.” There is some issue as to whether the Commission is authorized to impose such a duty.¹⁴ Beyond that, it is not at all clear how an attorney could discharge the duty. Among other questions, must an attorney tell the client that its attorney is investigating it? Must the client pay for such an investigation? How deeply must the attorney probe before he or she has discharged any duty of investigation? And most importantly, how can the attorney square any duty to investigate his or her client with the bedrock duty to represent the client zealously within the bounds of the law? While an attorney surely cannot ignore what he or she knows, an attorney cannot simultaneously be a zealous advocate for a client while investigating it. We are concerned that, in these circumstances, the attorney’s duty to investigate (and concern for his or her compliance with any such legal obligation) would require the attorney to withdraw from the representation. Such a consequence would largely frustrate the purpose Section 307 is designed to achieve.

Inundating senior management with reports of merely suspicious activity will not maximize compliance with the federal securities laws. The audit committee is most likely to act effectively when it is presented with clear evidence of wrongdoing. The Commission should be careful to avoid an overly expansive reading of Section 307 that would have the perverse result of depriving those occasions in which reports are made of their significance to the audit committee. The Commission should recognize that “up-the-ladder” reporting requirements provide some disincentive for employees to seek legal advice in the first place. At least some managers may want to avoid scrutiny from senior management and the board of directors in equivocal situations. To the extent clients seek legal advice less often, they are less likely to follow the law. In imposing a reporting requirement, the Commission must weigh the likelihood of increased compliance with the law as a result of bringing certain situations to the attention of a corporation’s senior management and its board of directors against the likelihood of decreased compliance resulting from decreased consultation with lawyers.

We respectfully submit that imposing a reporting requirement only with respect to situations that are clear violations strikes the appropriate balance. A lower threshold, we fear, will impose duties upon attorneys that are uncertain and highly daunting. The result will be a level of increased reporting to senior management and audit committees that will actually disserve the public’s purposes and retard, rather than promote, compliance with the law.

Finally, we urge the Commission to describe the conditions that trigger an obligation to report up the ladder, as they would appear to a reasonable attorney in light of the attorney’s training, experience, and seniority. Attorneys should not be expected to spot issues they are not equipped to see. What the reasonable and experienced senior securities attorney may regard as a clear violation of law may appear different – or not appear at all – to an unseasoned attorney with a different expertise.

¹⁴ Nothing in the language of Section 307 remotely suggests the existence of such a duty. While Senator Corzine mentioned on the floor of the Senate that “[W]hen lawyers are aware of a potential violation, they do have a duty to investigate,” in the same remarks Senator Corzine mentioned that the obligation imposed by the statement arises “[w]hen lawyers know of illegal actions by a corporate agent . . .” 148 CONG. REC. S6556 (daily ed. July 10, 2002) (statement of Sen. Corzine). These remarks are not enough to impose a duty that is completely unsupported by the words of the statute.

In particular, junior attorneys should be able to rely on consultation with their seniors in forming views about a client's conduct.¹⁵ Indeed, such consultation should be encouraged. Senior attorneys will not be able to extinguish a junior attorney's reporting obligation by fiat; but junior attorneys should be permitted to rely heavily on the experience, expertise, and judgment of their supervising attorneys in reaching their own judgments as to whether the conduct is of the nature to require reporting. Similarly, internal counsel for an issuer should be able to rely on the judgments of outside counsel as to whether the circumstances trigger an obligation to report, provided the opinion was obtained in good faith.

III. The Commission's Rule Under Section 307 Should Follow Established Formulations of Materiality

We understand the phrase "material violations" to refer to the consequences rather than the nature of the violation.¹⁶ And in applying the term, we believe the Commission will use the traditional concepts of materiality.¹⁷ In particular, we would expect attorneys to be able to assess materiality of a violation in terms of its then-current interest to reasonable investors. Making materiality judgments is hard enough; it becomes insupportably difficult to the extent attorneys would be called upon to conjecture as to the likelihood of material consequences flowing from a violation.

IV. An Attorney Should Be Required To Report Violations Of "Fiduciary Duty" or "Similar Violations" Only To The Extent Those Violations Create Disclosure Obligations Under The Federal Securities Laws

In describing the bodies of laws the violations of which should give rise to an attorney's "up-the-ladder" reporting obligation, Congress did not specify what it meant by "fiduciary duty" or "similar violation." The terms are extraordinarily imprecise and susceptible to a huge range of interpretations. We urge that the Commission interpret these words in light of the scope of its direct regulatory authority and concern. We respectfully submit that the most sensible interpretation of these words, and the most sensible assertion of the Commission's authority, would be limited to violations of fiduciary duties and other laws to the extent those matters in turn implicate obligations arising under the federal securities laws.

Nothing in Section 307 or its legislative history suggests that it was intended to broaden the Commission's direct regulatory authority. Nothing suggests that, contrary to years of

¹⁵ Model Rules 5.1 and 5.2 outline the responsibilities of law firms and associates. Rule 5.2(b) allows more junior lawyers to rely on ethical determinations by their superiors: "a subordinate lawyer does not violate the Rules of Professional Conduct if that lawyer acts in accordance with a supervisory lawyer's reasonable resolution of an arguable question of professional duty." ABA/BNA LAWYERS' MANUAL ON PROFESSIONAL CONDUCT, American Bar Association and The Bureau of National Affairs, Inc. (2002), Rule 5.2.

¹⁶ This is the clear import of the legislative history. As Senator Edwards stated, "The obligation to report is triggered only by violations that are material—violations that a reasonable investor would want to know about." 148 CONG. REC. S6555 (daily ed. July 10, 2002) (statement of Sen. Edwards).

¹⁷ See Basic, Inc. v. Levinson, 485 U.S. 224 (1988); TSC Industries v. Northway, Inc., 426 U.S. 438 (1976). See also Staff Accounting Bulletin No. 99, 1999 WL 1123073 (1999) ("SAB 99").

Supreme Court precedent,¹⁸ Congress intended to entrust the Commission with the authority to enforce compliance with state law obligations of fiduciary duty, or that it intended to entrust to the Commission enforcement of state securities laws, fiduciary duties arising under state insurance laws, fiduciary duty obligations of state and federal banking laws, obligations arising under the Employee Retirement Income Security Act of 1974, or under any federal and state law other than the federal securities laws.

It would be odd indeed if Congress intended to expand the Commission's authority to regulate attorneys' activities in areas that are otherwise outside of the Commission's jurisdiction. Where Congress, for example, has not granted the Commission plenary regulatory or enforcement jurisdiction with respect to the banking laws, there would seem to be no sense in empowering the Commission to impose upon attorneys requirements designed to further compliance with those laws.¹⁹

Even if one were to attribute to Congress an unarticulated intention to regulate attorneys to foster legal compliance generally, it would be odder still to limit its authority, as the statute explicitly does, to instances in which the attorney practices before the Commission. If the purpose is to promote compliance with, say, state fiduciary law doctrines, it should make no difference whether or not the attorney involved practices before the Commission.

But *disclosure* of violations of various bodies of law can be of central concern to the federal securities laws and thus the Commission's mission and authority. We believe that there is an interpretation of "fiduciary duty" and "similar violation" that would give full effect to the Commission's regulatory mission while not requiring the Commission to undertake attenuated and fragmentary enforcement of other laws. Under the interpretation we propose, an attorney would be obligated to report up the ladder with respect to any violation of fiduciary duty or any similar violation to the extent the violation implicates reporting or other obligations arising under the federal securities laws. This, we believe, is the correct interpretation of the law.

This interpretation is grounded in the language of the statute. The meaning of the first category of violations, the securities laws, is defined by statute to refer to the federal securities laws. Section 2(a)(15) of the Sarbanes-Oxley Act incorporates the definition now set forth in Section 3(a)(47) of the Exchange Act, as well as the rules, regulations, and orders implementing those statutes. The definition in the Exchange Act refers only to the federal securities laws.²⁰ The reference to "fiduciary duty" makes clear that the attorney must look not only to statutory

¹⁸ See Santa Fe Industries, Inc. v. Green, 430 U.S. 462 (1977); Virginia Bankshares, Inc. v. Sandberg, 501 U.S. 1083 (1991); Wharf (Holdings) Ltd. v. United Int'l Holdings, Inc., 532 U.S. 588 (2001); and SEC v. Zanford, 122 S.Ct. 1899 (2002).

¹⁹ Indeed, attorneys advising clients in those areas are unlikely to be engaged in practice before the Commission.

²⁰ See Exchange Act, 15 U.S.C. §78c (1934). "The term 'securities laws' means the Securities Act of 1933 (15 U.S.C. 77a *et seq.*), the Securities Exchange Act of 1934 (15 U.S.C. 78a *et seq.*), the Public Utility Holding Company Act of 1935 (15 U.S.C. 79a *et seq.*), the Trust Indenture Act of 1939 (15 U.S.C. 77aaa *et seq.*), the Investment Company Act of 1940 (15 U.S.C. 80a-1 *et seq.*), the Investment Advisers Act of 1940 (15 U.S.C. 80b *et seq.*), and the Securities Investor Protection Act of 1970 (15 U.S.C. 78aaa *et seq.*)."

law in determining what violations implicate the federal securities law, just as the term “similar violations” takes its meaning from the terms that precede it.

This is also an interpretation that would enable the Commission to give full effect to the statutory language without having to make – with no guidance in the statute or the legislative history – fine distinctions among the entire corpus of state and federal law as to which violations involve breaches of fiduciary duty and which are “similar.” Indeed, other than the one described above, it is hard to imagine an organizing principle under which it would do so.

Finally, the interpretation we suggest also would ensure that the obligations imposed on attorneys for SIA member firms are manageable. These attorneys should not be left to make judgments about the scope of their responsibilities with respect to bodies of law of which they have no knowledge and that are otherwise utterly inapplicable to their regular practice.

V. The Commission Should Avoid Putting Reporting Attorneys At Risk For Evaluating Whether A General Counsel’s Or Chief Executive Officer’s Response Is “Appropriate”

Having reported to a client’s general counsel or chief executive officer, an attorney may refrain from reporting to the board of directors only if the officer’s response is “appropriate.” Inevitably, the reporting attorney will have thrust upon him or her the responsibility to evaluate “appropriateness.” To avoid placing attorneys in untenable positions, and to avoid the very real risk of over-reporting to the audit committee or the board of directors, the Commission should specify with precision what types of responses are appropriate.

In particular, reporting attorneys should be able to rely on facially credible responses from their superiors. Here again, the threshold that triggers the reporting obligation is critical. If the attorney must report when he or she “knows” of the existence of a violation, the only action that should extinguish that obligation is a credible assertion from senior management that the violation has been stopped. Assuming that the attorney does not otherwise “know” that the violation is ongoing, an attorney should not be in the position of having to investigate beyond the client’s facially credible assertion.

Matters get more complicated if an attorney is required to report upwards on the basis of suspicion. What should the attorney do in the face of an assertion by the issuer’s general counsel or chief executive officer that each has looked into the matter and found that there is no factual basis for concern? Similarly, what should the attorney do in the face of an assertion by the general counsel that, after extensive research, the general counsel has concluded that the conduct does not amount to a violation of law? We submit that, unless the attorney “knows” to the contrary, he or she must be able to rely on these assertions. Otherwise, the attorney will be put into the untenable position of conducting an extended investigation of the client, with the practical consequence that the reporting obligation will be turned into an exercise of buck-passing by rote.

Similarly, the Commission should interpret “appropriate” to refer only to the issuer’s legal obligations. Anything beyond that is also beyond the attorney’s ken and his or her responsibilities as counsel. Reporting attorneys should not be put to the test of determining whether the issuer’s response is “appropriate” from a management or corporate governance

perspective. Attorneys simply have no special expertise or duties with respect to non-legal judgments.

Conclusion

We hope that these observations are helpful to the Commission. If you have any questions, please contact George Kramer of the SIA staff at 202-326-5316 or gkramer@sia.com.

Sincerely,

Howard E. Steinberg

Chair, SIA Ad Hoc Committee on
Section 307 of the Sarbanes-Oxley Act

Committee Members include:

Colleen Curran, American Express Financial Advisers, Inc.

Joseph Polizzotto, Lehman Brothers, Inc.

Kenneth L. Josselyn, Goldman, Sachs & Co.

Michael Stone, Morgan Stanley Dean Witter Inc.

Richard H. Walker, Deutsche Bank Inc.

Cc: Chairman Harvey L. Pitt
Commissioner Paul S. Atkins
Commissioner Roel C. Campos
Commissioner Cynthia A. Glassman
Commissioner Harvey J. Goldschmid