

## 77 Law Firms

December 18, 2002

Jonathan G. Katz, Secretary,  
Securities and Exchange Commission,  
450 Fifth Street, N.W.,  
Washington, D.C. 20549-0609.

Re: Sarbanes-Oxley Act § 307 – Implementation  
of Standards of Professional Conduct for  
Attorneys - Part 205 (File No. 33-8150.wp)

Dear Mr. Katz:

The undersigned 77 law firms (see pp. 8-10) are writing to express our concerns about certain aspects of proposed Part 205.

Whatever the merits, or the Commission's views on the merits, of involving the Commission in the regulation of a segment of the legal profession in each of the States and the District of Columbia, we recognize that Congress has given the Commission a mandate to adopt rules in this area within an unreasonably short timeframe. However, we urge the Commission not to go beyond what is absolutely required to be done before January 26 and to allow additional time for more widespread and thoughtful comment before determining whether more is required.

We strongly recommend that the Commission take no action prior to the January 26 deadline with respect to the following areas:

- Regulation of the Legal Profession Through “Noisy Withdrawal” Requirements
- Non-U.S. Lawyers

With respect to matters that the Commission is required to address by January 26, our concerns principally relate to issues arising from the extremely broad definitions proposed for the following terms:

- “Awareness of Evidence of a Material Violation”
- “Attorney”

- “Appearing and Practicing Before the Commission”
- “In the Representation of an Issuer”

Finally, we are very concerned by the potential serious adverse effects that Part 205, as currently proposed, may have on attorney-client relationships and on advocacy by attorneys acting on behalf of issuers before the Commission.

### **I. Deferring Action on Certain Matters**

Regulation of the Legal Profession Through “Noisy Withdrawal” Requirements. Lawyers are primarily regulated by the courts of the jurisdictions in which they practice. The rules governing lawyers are derived largely from the Model Rules of Professional Conduct and Model Code of Professional Responsibility but differ somewhat from state to state. The subject of a lawyer’s responsibilities with respect to a client who is in the process of committing, or may be about to commit, a financial wrong has been hotly debated in the profession for a number of years, continues to be the subject of strong disagreement and is being actively addressed by the American Bar Association. The resolution of this issue – for all lawyers and not just the subset practicing securities law – will necessitate a careful balancing of, on the one hand, the public policy that recognizes the right to effective counsel and the need for clients to be able to be candid with their counsel and, on the other hand, the policy that favors prevention of financial harm to the investing public in situations that the Commission has characterized as “extraordinarily rare”.

In the vast majority of cases counsel enjoy the confidence of their clients and, given access to the facts by their clients, succeed in persuading their clients to refrain from actions that harm the investing public. If clients are afraid to confide candidly and completely in their counsel and instead proceed without the advice of counsel, the public will inevitably be harmed in some cases when it need not have been. Or clients may be prompted to avoid cautious and prudent counsel, with the same result. The basic force for conformance of business conduct to legal norms is a strong and independent Bar that enjoys the trust and confidence of its clients.

Furthermore, on an issue as sensitive and important as this one we believe the State courts have – and should have – a primary and broad jurisdiction with respect to all lawyers practicing within their jurisdictions. We believe the Commission requires more explicit authority from Congress before it attempts to preempt State court jurisdiction. Even if the Commission is right in concluding that its rules preempt State court rules, we are concerned that securities lawyers may face conflicting duties under Commission-made and court-made rules. The scope of the Commission rules – insofar as they cover “breach of fiduciary duty or similar violation” – will be unclear. In the face of this uncertainty, lawyers simply will not know which rules apply.

We believe the proposed requirement that lawyers and, as a result, law firms in certain circumstances withdraw from representing the issuer is contrary to the legislative history of Sarbanes-Oxley Act § 307 and, from the perspective of both the issuer and the lawyers forced to withdraw, punitive in nature. To the extent the requirement is intended to force a law firm to withdraw from unrelated representations (e.g., all litigation, tax advice, etc.), it is unreasonable, disruptive and unworkable. Withdrawal from litigation without court approval could violate court rules, not only ethical rules. Moreover, assuming that successor counsel learns what the withdrawing counsel knows (and, under the Commission's proposal, the client would be required to tell successor counsel the reason for the withdrawal), in the circumstance presented by the Commission the client could, as a practical matter, have a very difficult time finding a lawyer to represent it. The threat of withdrawal thus may effectively force a client to acquiesce in following the lawyer's advice even when in good faith it strongly disagrees with the advice and the advice may even be wrong or highly debatable.

We are also concerned about the potential effects of a noisy withdrawal on the attorney-client relationship and the attorney-client privilege. In particular, we question whether, even if the Commission has been given the authority to preempt State ethical rules concerning a lawyer's conduct, that authority is broad enough to permit, at the same time, preemption of the Federal Rules of Evidence as well as all applicable State evidentiary rules regarding the attorney-client privilege and attorney work-product protection.

Requiring lawyers to report outside the attorney-client relationship presents complex issues (including, at least in a criminal investigation context, serious potential constitutional issues under the Sixth Amendment) and has the potential fundamentally to affect that relationship. While Congress is requiring the Commission to act quickly on matters within the scope of § 307, it is not forcing the Commission to resolve that issue by January 26, or indeed at all. The Commission should not rush to act on noisy withdrawal.

Non-U.S. Lawyers. In proposing to extend Part 205 to non-U.S. lawyers, we believe the Commission is again proposing to go beyond what the statute requires. At December 31, 2001, 1,344 companies from 59 countries were reporting issuers under the Exchange Act. Local lawyers in these countries are subject to a wide variety of professional regulatory regimes, some of which are quite different from the regulatory regime in the United States. In most cases they are not licensed to practice in the United States, have no knowledge of U.S. securities law and do not advise as to U.S. securities law. They may not even speak or read English. Non-U.S. issuers and their external and internal local lawyers usually rely on U.S. counsel as to the interpretation and application of U.S. securities law matters. Whatever the Commission's views of its authority to preempt State law, it cannot preempt conflicting foreign professional requirements for lawyers. In addition, applying Part 205 to non-U.S. lawyers will simply add to the

disincentives foreign companies have to register their securities under the Exchange Act, which is not in the interest of the investing public.

We believe that, as a matter of international comity, the Commission should refrain from attempting to exercise jurisdiction over a portion of the legal profession in foreign countries. Instead, the Commission should take sufficient time to consult with members of the foreign bars as well as foreign regulatory authorities to determine whether there is an approach that achieves the objectives of Sarbanes-Oxley Act §307 while, at the same time, avoiding the numerous issues raised with respect to non-U.S. attorneys. The problem is substantially compounded by the breadth of the definitions of “attorney” and “appearing and practicing before the Commission”. We believe the comment period allotted for Part 205 is not sufficient for interested persons, including foreign regulators and lawyers, to express their views on these extremely complex issues, especially in light of the holiday season.

In addition, there are many lawyers admitted to practice in the United States that work in the non-U.S. offices of U.S. and foreign law firms or companies. Many of these lawyers, either because they themselves are also admitted to practice in a foreign jurisdiction or because their firms are so admitted, are also subject to the laws and ethical codes applicable to lawyers in such jurisdictions. They are, in a sense, both U.S. lawyers and non-U.S. lawyers. We believe that, for the reasons described in the previous paragraph, the Commission should take additional time to determine how the objectives of Sarbanes-Oxley Act §307 may be achieved with respect to this group of lawyers.

## **II. Breadth of the Proposed Definitions**

While we understand the Commission’s desire to cast a wide net to catch all improper behavior, we believe that the approach taken in Part 205 is both unworkable and inappropriate. The extremely broad proposed definitions of key terms in Part 205 create an extraordinary level of ambiguity. This ambiguity results, in large part, from the use of terms that expand the coverage of the proposed rules, and attempt to apply a reasonableness standard, to individuals who, through neither negligence nor improper behavior, may not know they are covered by the rules, may be unlikely to grasp the significance of certain information they receive regarding an issuer or may be unable to assess such information in a manner that would further Congress’s objectives under Sarbanes-Oxley Act § 307. While Part 205 seems to recognize these issues insofar as its enforcement mechanism would punish only serious violations, we believe this is not an appropriate approach to regulation of lawyers. Particularly in light of the consequences for clients and lawyers of complying with the procedures required by Part 205, we believe it is imperative for the final rules to be clear in both their coverage and application.

“Awareness of Evidence of a Material Violation”. The proposed rules require action by a lawyer when he or she becomes “aware” of “information” that would

lead an attorney “reasonably” to believe a “material violation” has occurred or is about to occur. “Material” is defined as conduct or information about which “a reasonable investor would want to be informed before making an investment decision”, which differs from the existing definitions of “material” in Securities Act Rule 405 and Exchange Act Rule 12b-2 (“substantial likelihood that a reasonable investor would attach importance in determining whether to buy or sell”), thereby raising interpretive issues.\* “Material violation” covers, in addition to violations of federal and state securities laws, breaches of common law fiduciary duty, including malfeasance, nonfeasance, abdication of duty, abuse of trust and approval of unlawful transactions. It also covers any “similar material violation,” a term so vague even the Commission is unwilling to attempt to define it.

We believe the Commission’s attempt to create an objective standard is flawed in several respects. It is difficult to determine what portion of the required determination by an attorney is meant to be objective. The Commission has, we believe correctly, rejected a “should have known” standard and an obligation on the part of an attorney to investigate. Assuming that the lawyer is, in fact, aware of evidence of a possible violation and is not obligated to investigate, the issue then becomes the nature of the required assessment of the information that the lawyer has actually acquired. That assessment should be evaluated in the context of what the lawyer has actually come to know and believes, not what some hypothetical objectively reasonable lawyer might conclude.

We believe an objective “reasonable lawyer” standard as to the assessment of the information acquired by an attorney is not appropriate or required by the Sarbanes-Oxley Act. Imposing such an objective standard on a lawyer’s assessment of information would shift the Commission’s role from one of policing lawyer ethics to one of policing lawyer competence. If the Commission wishes to stay true to Congress’ directive to implement rules regulating lawyer ethics, then the appropriate standard should be one that is based on whether an attorney actually becomes aware that the issuer is undertaking actions that would clearly constitute a material violation of law. Such a standard would be more consistent with the Commission’s use, in the definition of “evidence of a material violation,” of the phrase “would lead” rather than “could lead” and the statements in the proposing release that an attorney’s reporting obligations are not

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\* It also differs from the U.S. Supreme Court’s formulation: “substantial likelihood that a reasonable shareholder would consider it important,” “substantial likelihood that ... the omitted fact would have assumed actual significance in the deliberations of the reasonable shareholder” and “substantial likelihood that the disclosure ... would have been viewed by the reasonable investor as having significantly altered the ‘total mix’ of information”. TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976).

triggered until the attorney “can be sure” that the issuer will actually pursue a course of action that is “clearly illegal”.

Although the proposed rules purport to impose an objective standard, the Commission also recognizes that the standard actually applied must differ from lawyer to lawyer because attorneys cannot be “expected to identify issues they are not equipped to see”. Whether or not a violation has occurred or (even more conjectural) is about to occur is not subject to a bright-line or litmus test. Reasonable lawyers may disagree. The opportunities for second-guessing a lawyer’s good faith judgment are legion, and the consequences of being judged wrong after the fact are devastating, as a violation of Part 205 is a violation of the Exchange Act and can subject the lawyer to discipline by the Commission. And if a lawyer errs on the side of caution, takes steps that he or she believes are required or permitted to be taken by the proposed rules that are inconsistent with State ethical rules and is judged wrong as to the reasonableness of his or her belief (i.e., the proposed rules do not preempt State rules if the proposed rules are judged to be inapplicable), the lawyer may be subject to malpractice, defamation and other claims or discipline under the State standards. As noted above, the problems faced by non-U.S. attorneys are even more severe.

“Attorney”. According to the proposing release, the proposed rules are intended to cover a licensed attorney who is no longer acting in his or her capacity as a lawyer, e.g., an investment banker working on a financing transaction who happens to have a law degree, or a director who happens to have a law degree, in each case merely because he or she maintained his or her Bar membership. We are confident that Sarbanes-Oxley Act § 307 does not require such an expanded concept of an “attorney”. Moreover, such an expansive definition of the term “attorney” is not necessary to achieve the purposes of the Commission’s mandate and only serves to make the application of Part 205 unworkable. We believe Part 205 should be limited in its application to attorneys representing an issuer in a legal capacity.

The proposed rules are problematic in their application to lawyers practicing in law firms. While the “up-the-ladder” and “noisy withdrawal” obligations appear to be obligations of the individual lawyer, in a law firm context the clients are clients of the firm rather than any individual lawyer, and often several lawyers of varying seniority work on any given matter. In addition, the proposed rules attempt to deal with subordinate/superior relationships, but their operation within a law firm is far from clear. This creates uncertainty with respect to up-the-ladder obligations in the law firm context and becomes extremely problematic if withdrawal is required. We urge the Commission to provide the flexibility under the proposed rules for a law firm to design and implement procedures for the administration of reporting with respect to firm clients.

“Appearing and Practicing Before the Commission”. A rule designed to encourage good disclosure by an issuer should encourage wide review of that disclosure by those acting on behalf of the issuer. Indeed, this is a core principle of the

Commission's concept of "disclosure controls and procedures". We believe the proposed rules should not apply to lawyers who have advised as to a limited aspect of the disclosure contained in a registration statement or report filed with the Commission, such as lawyers representing the issuer in litigation who are asked by disclosure counsel to comment on descriptions of the cases they are handling. As proposed, Part 205 discourages wide review, particularly by "attorneys" (in whatever capacity they might actually be serving), and may even encourage attorneys to avoid opportunities to review documents. Creating incentives contrary to the goal of good disclosure can hardly be in the interest of the investing public. A less counterproductive approach would be to limit the application of the rules to an attorney who has prepared a "substantial" portion, or who has had "substantial" participation in the process of preparing a "substantial" portion, of any disclosure document that the attorney knows is being prepared for the purposes of being filed with, or incorporated into a registration statement or report being filed with, the Commission.

We believe the Commission overreaches when it attempts to assert jurisdiction over lawyers who advise that the securities laws do not apply or an exemption is available and over lawyers who draft documents that are not prepared for the purpose of being, but eventually may be, filed with the Commission, such as exhibits to a registration statement (e.g., material contracts, benefit plans).

"In the Representation of an Issuer". The Commission should not, and its mandate does not require it to, regulate a lawyer retained by a third party whose work may or happens to provide a benefit to a company. We believe that "up the ladder" and "noisy withdrawal" do not work in the case of third parties' counsel whose work for, and advice to, the third party may benefit the company. Is an attorney to go "up the ladder" inside a non-client, and how does an attorney withdraw from a non-existing relationship? A company will be at the risk of the competence (knowledge, experience and judgment) of all the counsel chosen by third parties whose advice might benefit the company. The definition is so broad that it might be read to cover attorneys who, as counsel to third parties, review and comment on documents prepared by a company or its counsel and thereby happen to benefit indirectly the company. We urge the Commission to clarify in the final rules that counsel to third parties are not covered by the rules and that the rules apply only when the attorney is retained, engaged or employed by the company to provide legal advice or services to the company and the § 307 issue arises in the course of the attorney's representation of the company.

### **III. Effect on Advocacy**

We believe the Commission should be very careful in how it exercises the authority over lawyers that has been given it by Congress. We are concerned that Part 205 would drive a wedge between client and the counsel who advised it on a matter by creating a conflict of interest between the client and its counsel and forcing the client to use other counsel to defend itself. We are also concerned the explicit or implicit threat

of enforcement of “ethics” rules by the Commission staff could chill a lawyer’s energetic representation of his or her client, thereby endangering the right to effective counsel. We believe that, in a nation governed by law, lawyers representing clients before a regulator should not have to rely on the discretion of that very regulator to restrain itself from interfering with the effectiveness of that representation.

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Given the extremely short time for comments and the circumstances of this letter, it is not intended to be, and is not, a comprehensive analysis of all the problems inherent in Part 205 as proposed. Additional matters will be addressed separately by the participating firms.

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The Commission must do what it is required by the statute to do. But we urge the Commission to exercise caution and restraint in going beyond that point and, if it believes it must, to do so in a more orderly and deliberate manner.

Respectfully submitted,

Akin Gump Strauss Hauer & Feld L.L.P.  
Alston & Bird LLP  
Arnold & Porter  
Baker Botts L.L.P.  
Ballard Spahr Andrews & Ingersoll, LLP  
Brobeck, Phleger & Harrison LLP  
Bryan Cave LLP  
Cadwalader, Wickersham & Taft  
Cahill Gordon & Reindel  
Chadbourne & Parke LLP  
Cleary, Gottlieb, Steen & Hamilton  
Clifford Chance  
Covington & Burling  
Cravath, Swaine & Moore  
Davis Polk & Wardwell  
Day, Berry & Howard LLP  
Debevoise & Plimpton  
Dechert  
Dewey Ballantine LLP  
Dorsey & Whitney LLP  
Drinker Biddle & Reath LLP

Faegre & Benson LLP  
Fenwick & West LLP  
Foley & Lardner  
Fried, Frank, Harris, Shriver & Jacobson  
Fulbright & Jaworski L.L.P.  
Gardner Carton & Douglas  
Gibson, Dunn & Crutcher LLP  
Goodwin Procter LLP  
Hale and Dorr LLP  
Hogan & Hartson L.L.P.  
Hughes Hubbard & Reed LLP  
Hughes & Luce, L.L.P.  
Hunton & Williams  
Jones Day  
Katten Muchin Zavis Rosenman  
Kaye Scholer LLP  
Kilpatrick Stockton LLP  
King & Spalding  
Latham & Watkins  
LeBoeuf, Lamb, Greene & MacRae LLP  
Linklaters  
Mayer, Brown, Rowe & Maw  
McDermott, Will & Emery  
Milbank, Tweed, Hadley & McCloy LLP  
Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C.  
Morgan, Lewis & Bockius LLP  
Morris, Manning & Martin, LLP  
Munger, Tolles & Olson LLP  
O'Melveny & Myers LLP  
Orrick, Herrington & Sutcliffe LLP  
Osler, Hoskin & Harcourt LLP  
Palmer & Dodge LLP  
Paul, Weiss, Rifkind, Wharton & Garrison  
Pepper Hamilton LLP  
Pillsbury Winthrop LLP  
Piper Rudnick LLP  
Powell, Goldstein, Frazer & Murphy LLP  
Preston Gates & Ellis LLP  
Proskauer Rose LLP  
Ropes & Gray  
Schiff Hardin & Waite  
Shearman & Sterling  
Sidley Austin Brown & Wood LLP

Simpson Thacher & Bartlett  
Skadden, Arps, Slate, Meagher & Flom LLP  
Squire, Sanders & Dempsey L.L.P.  
Sullivan & Cromwell  
Testa, Hurwitz & Thibault, LLP  
Torys LLP  
Wachtell, Lipton, Rosen & Katz  
Weil, Gotshal & Manges LLP  
White & Case LLP  
Willkie Farr & Gallagher  
Wilson Sonsini Goodrich & Rosati, Professional Corporation  
Winston & Strawn  
Wolf, Block, Schorr and Solis-Cohen LLP

cc: Hon. Harvey L. Pitt, Chairman  
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Giovanni P. Prezioso, General Counsel  
Alan L. Beller