



April 17, 2003

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

Re: Proposed Rules of Conduct for Attorneys, File No. S7-45-02

Dear Mr. Katz:

We are submitting separate views in response to the request for comment by the Securities and Exchange Commission ("Commission") in Release No. 33-8186 (January 29, 2003), 68 FR 6324 (February 6, 2003) ("Proposing Release") on the "noisy withdrawal" provision of the Commission's proposed rules concerning professional conduct of attorneys who appear and practice before the Commission contained in Release No. 33-8150 (November 21, 2002), 67 FR 71670 (December 2, 2002) ("Original Release") and on what may be called the "issuer reporting alternative" to those provisions proposed in the Proposing Release.<sup>1</sup> In passing, we also comment on certain aspects of the conduct rules as they have been adopted by the Commission in Release No. 33-8185 (January 29, 2003), 68 FR 6296 (February 6, 2003).

The "Noisy Withdrawal" Provision. We concur with several of the reasons articulated by others for urging the Commission to back away from its original proposal to require, under certain circumstances, a lawyer who appears and practices before the Commission to withdraw from representing an issuer, notify the Commission of that withdrawal, and disaffirm documents submitted to or filed with the Commission ("noisy withdrawal").<sup>2</sup> Among the most persuasive of

<sup>1</sup> We submitted our own letter in response to the Original Release (see letter to Jonathan G. Katz, Secretary, Commission, from Schiff Hardin & Waite, dated December 18, 2002 ("SH&W Letter")), joined in the letter to the Commission addressing the Original Release submitted by seventy-seven law firms, dated December 18, 2002, and joined in the letter to the Commission responding to the Proposing Release submitted on behalf of seventy-six law firms, dated April 7, 2003.

We recognize that the formal deadline for submission of comments responding to the Proposing Release has passed, but hope that sufficient time still remains to permit consideration of these comments in the context of the Commission's ongoing review of its conduct rules for lawyers.

<sup>2</sup> See, e.g., Letter to the Commission from Alfred P. Carlton, Jr., President, American Bar Association, dated December 18, 2002 ("ABA Letter"); see also letter to the Commission from Alfred P. Carlton, Jr., President, American Bar Association, dated April 2, 2003.

those reasons is the certainty that such a requirement would chill the willingness of issuers' managements to consult openly and fully with counsel as to matters that management is concerned – rightly or wrongly – do or might reveal a “material violation” (within the meaning of Section 205.2(i) of Part 205 of the Code of Federal Regulations) that is ongoing or about to occur unless the issuer undertakes what the lawyer regards as an appropriate response or refrains from whatever future conduct the lawyer believes is likely to involve a material violation.<sup>3</sup> It is painfully obvious that such interference with the traditional cloak of secrecy available to clients that protects their communications with their lawyers from scrutiny by others must lead to fewer candid revelations to lawyers of information that now leads to the delivery of sound advice and often avoids or produces remediation of unlawful conduct – all without the involvement of the mechanisms of government.

We believe that, whatever positive gains might flow from adoption of the “noisy withdrawal” provision by requiring lawyers to alert the Commission and, thus, investors to the possibility that their issuer clients have engaged or are about to engage in material violations, much more will be lost. This is so, we think, because members of issuers' managements will no longer be able to discuss sensitive matters with their legal counsel in complete confidence. They necessarily will have to weigh the risks of revealing what may be material violations to their lawyers and face the possibility of subsequent notice to the Commission of those revelations by their own counselors, albeit indirectly, if the issuer does not do whatever its lawyer concludes is necessary to do (or refrain from doing) to remedy (or avoid) what the lawyer regards as violations, against the risks of proceeding without informed legal advice. Under these circumstances, as indicated in our earlier letter, we think that the net result is likely to be more unlawful conduct rather than less.<sup>4</sup>

We also are troubled by the inherent difficulty of insisting on such a requirement in the context of law firm representation of issuers, difficulties that the Commission has yet to acknowledge and that do not seem to us to be amenable to ready resolution. Virtually all issuers engage law firms rather than individuals as their counsel. One can expect law firms to adopt appropriate internal procedures contemplating collective analysis of situations where a single lawyer within the firm believes that he or she has become aware of evidence of a material violation by an issuer client of the firm. The Commission's conduct rules, however, do not come *to grips* with the fact that it is the single lawyer's law firm rather than that lawyer that has been engaged by the issuer. When a single lawyer continues to believe, against the collective judgment of other competent and prudent lawyers within the firm -- as must be expected to happen at least from time to time -- that a client is engaging or is about to engage in an ongoing

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<sup>3</sup> See, e.g., ABA Letter at 26.

<sup>4</sup> See SH&W Letter at 2.

or imminent material violation, it should not be expected that the firm will withdraw from representing that issuer simply because of that single lawyer's disagreement.<sup>5</sup>

Finally, we note that, quite apart from what we perceive as difficulties under the proposed conduct rule flowing from the fact that publicly owned issuers typically engage law firms rather than individual lawyers, the withdrawal provision of the proposed conduct rule would require complete withdrawal from representation of an issuer notwithstanding that much of the work being performed for that issuer may have nothing whatsoever to do with the material violation suggested by the evidence to be reported (which, if the report does not receive what the reporting lawyer regards as an appropriate response, triggers the withdrawal obligation). This seems wholly inappropriate to us.

We urge the Commission to abandon the "noisy withdrawal" provision because, in any form, it is intrinsically inimical to sound lawyer-client relationships and will defeat the overall good that flows from the ability of clients to convey *to* their lawyers, with unfettered candor and openness, the facts and circumstances that shape the lawyer's judgment and advice.

The Issuer Reporting Alternative. While the proposed issuer reporting requirement alternative to the "noisy withdrawal" provision superficially solves the problem of compelling lawyers who appear and practice before the Commission to signal to the Commission and to the market that credible evidence exists to the effect that their former clients have engaged or are about to engage in material violations of the law (in contravention of basic notions of attorney-

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<sup>5</sup> Without such withdrawal, of course, there can be no triggering of the notice and document disaffirmance elements of the Commission's proposed "noisy withdrawal" provision. We also note with respect to the law fit-individual lawyer issue that documents concerning the issuer implicated by a suspected material violation that have been prepared by outside counsel (or that are based on or incorporate such outside counsel's work) and have been supplied to or filed with the Commission, either directly by such counsel or indirectly by the issuer, will have been prepared by the individual lawyer on behalf of his or her law firm, not by the individual on his or her own behalf.

It may be that the individual lawyer who disagrees with his or her firm's conclusions about what that lawyer regards as a material violation should withdraw from further participation in the firm's representation of the issuer under such circumstances -- or even, in extreme cases, resign from the firm. Sound law firm procedures today often contemplate such withdrawals when a particular representation does not and cannot be expected to command a particular lawyer's zeal, for example, for reasons of conscience (e.g., a firm's pro bono representation of an accused child molester where a particular lawyer assigned to the matter is the parent of a child victim of molestation). No individual lawyer within a law firm, however, should be expected or required to "blow the whistle" on his or her firm or the firm's client to the Commission under these circumstances.

client confidentiality), it does very little to cure the essential flaws in or avoid the foreseeable harms of the “noisy withdrawal” proposal.

The alternative still would require the lawyer to withdraw from representing the issuer after reporting what appears to the lawyer to be evidence of a material violation unless the lawyer receives what he or she regards as an appropriate response.<sup>6</sup> Further, the alternative does nothing to address or resolve the law firm/individual lawyer problem discussed above in connection with “noisy withdrawal.”

Upon receiving notice of *the* lawyer’s withdrawal, the issuer, rather than the lawyer, would be required to report it to the Commission and the market even if the issuer in good faith were to disagree with the conclusions of its former counsel. The obligation to make such a report would result, in our view, in the same severe erosion of trust and confidence by managements in their issuers’ lawyers and have the same undesirable consequences pointed out above in connection with the “noisy withdrawal” provision. Thus, we conclude that it is not in the public interest to adopt the issuer reporting alternative and recommend that it be rejected.

Underlying Considerations. We appreciate that recent times have been plagued by disgraceful conduct by the highest levels of a number of our publicly owned companies, with grave damage to investors in those companies and investor confidence generally. We acknowledge that some independent auditors, and perhaps even some investment banking firms and lawyers for those companies, must accept a portion of the blame for facilitating or tolerating that conduct if not actively advancing it. Congress has prescribed remedies addressing such misbehavior, uncovered in its investigations of these scandals, in the Sarbanes-Oxley Act (“SOXA”) and the Commission has done what has been asked of it by that legislation to implement those remedies.

What interests are at stake in the context of considering further amendment of the Commission’s practice rules for lawyers who appear and practice before it in connection with representation of publicly owned issuers? It can be argued that the integrity of the Commission’s processes, deterrence of lawyer misconduct, and protection of investors all are at issue. We

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<sup>6</sup> The consequence under the alternative, as noted above in connection with the “noisy withdrawal” provision, would be to force the lawyer to withdraw altogether as counsel *to* the issuer, regardless of how many other matters the lawyer or his or her firm may be involved in as counsel to that issuer -- even though other elements of the representation are unrelated to the matter affected by the material violation -- if (i) the lawyer reasonably concludes that there is substantial evidence that a material violation is ongoing or is about to occur and that it is likely, in the lawyer’s judgment, to cause substantial injury to the issuer, and (ii) the lawyer has not received what the lawyer regards as an appropriate response after reporting that evidence to the issuer. (One may question whether lawyers are equipped or qualified to judge whether a material violation that is ongoing or about to occur is “likely” to cause substantial injury to the issuer no matter how many of them regularly appear on behalf of clients to argue that such an injury has or has not occurred on the basis of evidentiary facts.)

conclude, however, that adoption of the “noisy withdrawal” provision or the issuer reporting alternative would do little to bolster the Commission’s integrity (to the extent it is truly implicated at all in this context), succeed only in convincing issuer clients that lawyers’ understandable fear of engaging in misconduct under the new rules may well make them dangerous to consult, and reduce rather than advance the goal of investor protection.

In the latter regard, one can only shudder at the prospect of the market impact of discovery that an issuer’s lawyer or law firm has withdrawn from representing that issuer “for professional reasons” – something the provision would require even given the good faith disagreement of the issuer’s management and, worse, even though a tribunal at a later time (after stockholder value has been destroyed) might disagree with the assertion by a lawyer that there is or was evidence of a material violation in the first place or that the lawyer’s view that the issuer did not properly respond to a report of such evidence was **wrong**. If the lawyer’s judgment in such cases is right, perhaps nothing can or should protect existing investors from a calamitous market reaction. If the lawyer turns out to be wrong, however, something that may take very substantial time to determine, grave harm will have been done for very little reason – that is, solely because of an off-base, but publicly trumpeted conclusion of a former counsel to the issuer.<sup>7</sup> Is this not a strong reason, among others, why enforcement investigations by the Commission’s staff are a carefully guarded secret until and unless a settlement is **reached** or the Commission determines to open a formal investigation?

Neither the “noisy withdrawal” provision nor the issuer-reporting alternative was contemplated by SOXA. On their merits, both initiatives by the Commission seem to us to be unnecessary and ill advised. Neither should be adopted.

We would be pleased to further discuss our views with respect to the Proposing Release with the Chairman, any Commissioner, or any member of the staff involved in consideration of amendment of the Commission’s conduct rules for lawyers who appear and practice before the Commission.

Sincerely,

SCHIFF HARDIN & WAITE

By:   
Andrew M. Klein

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<sup>7</sup> Nothing of importance can be done about this risk by changing the standard to be applied in deciding whether evidence of a material violation in fact exists – e.g., by triggering the withdrawal and reporting obligations only upon discovery of what the lawyer “concludes” is “substantial” evidence.

Jonathan G. Katz

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cc: Hon. William H. Donaldson, Chairman  
Hon. Paul Atkins, Commissioner  
Hon. Roel Campos, Commissioner  
Hon. Cynthia A. Glassman, Commissioner  
Hon. Harvey Goldschmid, Commissioner  
Giovanni P. Prezioso, General Counsel  
**Alan** L. Beller, Director  
Division of Corporate Finance and Senior Counselor to the Commission

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