Bloomberg BNA

Securities Regulation & Law Report™

WHISTLEBLOWERS

Attorneys Caught in the Ethical Crosshairs: Secretkeepers as Bounty Hunters Under the SEC Whistleblower Rules



BY WILLIAM MCLUCAS, LAURA WERTHEIMER, AND ARIAN JUNE

Imagine you are counsel to a public company and are tasked with reviewing its annual 10-K. In the course of your review, you confer with a number of individuals in the finance and accounting functions and they report that a significant number of post-close adjustments were made at year end and these adjustments significantly improved the company's financial presentation. Because post-close adjustments can raise a red flag, you discuss the number and dollar value of the adjustments with the company's General Counsel. She responds that the company is committed to proper accounting and full disclosure and that she will investigate the propriety of the post-close adjustments. Later that week, she advises that all of the adjustments were driven by a change in the company's revenue recognition policies, which had been approved by the company's auditors, and that all of the adjustments had proper documentation. You suspect, but do not know, that the policies were changed so that the company could recognize more revenue and report a strong performance for the year and pay its senior executives cash bonuses. Existing draft language in the 10-K explains the change in the company's revenue recognition policies. You revise that language to underscore that the policies were changed at year end which permitted the company to recognize significant additional revenues and that bonuses were paid to the executive management team on the basis of the company's financial results for the year. The General Counsel includes your proposed revisions in the draft 10-K circulated to the CEO and to the Audit Committee of the company's Board. At the invitation of the Audit Committee, you attend its meeting where the draft 10-K is reviewed. You explain your concerns regarding the timing and effect of the changes to the company's revenue recognition policies and caution that the 10-K could be incomplete if it fails to clearly explain the effect of the changed policies on the company's revenue stream. The Audit Committee responds that these policy changes had been under consideration for almost

William McLucas, chair of WilmerHale's Securities Department, is a partner resident in the firm's Washington, DC, office. Laura Wertheimer is a partner resident in WilmerHale's Washington, DC office and a member of its Securities Department. Arian June is a counsel resident in WilmerHale's Washington, DC, office and a member of the Securities Department. Mr. McLucas may be reached at (202) 663-6622 or william.mclucas@wilmerhale.com. Ms. Wertheimer may be reached at (202) 663-6450 or laura.wertheimer@wilmerhale.com. Ms. June may be reached at (202) 663-6213 or arian.june@wilmerhale.com.

 ISSN 0037-0665

a year and were closely vetted by the company's external auditor and that the company had baked the expected additional revenue into its financial projections for the year. It declines to accept your suggested disclosures.

You reasonably believe that issuance of the 10-K without language along the lines of your draft could amount to a non-fraud civil violation of a federal securities law that will likely cause substantial financial injury to the issuer or investors. Can you blow the whistle and seek a Securities and Exchange Commission whistleblower bounty? The SEC thinks you can, even if the rules of professional conduct of the state(s) in which you are licensed do not permit you to disclose client confidences to a third party in these circumstances.

In the Adopting Release accompanying the SEC's whistleblower rules, the SEC recognized ''the prominent role that attorneys play in all aspects of practice before the Commission and the special duties they owe to clients'' and ''observed that compliance with the federal securities laws is promoted when individuals, corporate officers, and others consult with counsel about possible violations.''[1] Because ''[t]his important benefit could be undermined if the whistleblower award program created monetary incentives for counsel to disclose information about possible securities violations in violation of their ethical duties to maintain client confidentiality,''[2] the SEC asserted that its rules limit the ability of lawyers to become award seeking whistleblowers. It explained that a lawyer's eligibility for a whistleblower bounty was restricted to three limited circumstances: when disclosures were permitted by § 205.3(d)(2) of the SEC's standards of professional conduct for attorneys practicing before the Commission; when permitted by ''applicable state attorney conduct rules''; or ''otherwise.''[3] The SEC advised that these circumstances were ''consistent with the public policy judgments that have been made as to when the benefits of permitting disclosure are justified notwithstanding any potential harm to the attorney-client relationship.''[4]

Part I of this article reviews the contours of the permissive disclosures authorized by § 205.3(d)(2). Next, we compare the scope of disclosures allowed by § 205.3(d)(2) to the range of disclosures sanctioned by state rules. While most states have adopted exceptions to their confidentiality rules that would permit lawyers to report confidential information to a third party to prevent a crime or fraud, no state rule permits lawyers to disclose client information without consent to obtain a possible monetary bounty. Part II evaluates the strength of the SEC's position that the permissive disclosures authorized by § 205.3(d)(2) and incorporated into SEC Rule 21F-4(b)(4) preempt conflicting state rules that would bar such disclosures. Even assuming that a court were to find that Congress intended, in its adoption of Dodd-Frank Wall Street Reform and Consumer Protection Act, to delegate to the SEC the authority to preempt conflicting state confidentiality rules, Part III explains that other state rules, such as the conflicts rules, are not preempted and assesses the impact of state conflicts rules on a lawyer's ability to become an award-seeking SEC whistleblower. Last, Part IV offers a number of practical strategies for organizations subject to the Dodd-Frank whistleblower program to consider to reduce the threat that trusted fiduciaries will become SEC bountyhunters.

I. Lawyers as SEC Whistleblowers?

We have written previously about the eligibility requirements imposed by the SEC whistleblower rules.[5] One of those requirements is the provision of ''original information'' to the SEC. The SEC whistleblower rules make clear that a lawyer will not generally be credited with providing ''original information'' if that information was obtained in one of three ways:

(1) from confidential communications subject to the attorney-client privilege;

(2) from the legal representation of a client; or

(3) from association with a firm retained by an organization to conduct an inquiry into possible violations of law.[6]

The SEC explained that these exclusions to the definition of ''original information'' were warranted by ''the special duties [that lawyers] owe to clients. . . . [C]ompliance with the federal securities laws is promoted when individuals, corporate officers, and others consult with counsel about possible violations, and the attorney-client privilege furthers such consultation. This important benefit could be undermined if the whistleblower award program created monetary incentives for counsel to disclose information about possible securities violations in violation of their ethical duties to maintain client confidentiality.''[7]

However, these exclusions are not absolute. The SEC rules provide three exceptions to these exclusions, which permit a lawyer to act ''for [his] own benefit'' and seek a whistleblower bounty. A lawyer will satisfy the ''original information'' prong of the eligibility requirements when he or she submits information to the SEC where such disclosure is:

- permitted by § 205.3(d)(2);
- permitted by applicable state attorney conduct rules; or
- ''otherwise.''[8]

According to the SEC, these exceptions ''strike[] the right balance because these exclusions are consistent with the public policy judgments that have been made as to when the benefits of permitting disclosure are justified notwithstanding any potential harm to the attorney-client relationship.''[9]

We now discuss each of these exceptions.

---

[1] Implementation of the Whistleblower Provisions of Section 21F of the Securities Exchange Act of 1934, Release No. 34-64545, at 56 (May 25, 2011) (''*Adopting Release*''), *available at* http://www.sec.gov/rules/final/2011/34-64545.pdf.

[2] *Id*.

[3] *Id*.; SEC Rule 21F-4(b)(4)(i).

[4] *Adopting Release*, *supra* note 1, at 60.

[5] *See* Thomas White, Mary Jo Johnson, Douglas Davison & Arian June, *SEC Approves Sweeping Whistleblower Bounty Regime*, WilmerHale Client Alert, (May 27, 2011) available at http://www.wilmerhale.com/pages/publicationsandNewsDetail.aspx?NewsPubId=88609.

[6] SEC Rule 21F-4(b)(4)(i-ii) and (iii)(C), 17 C.F.R. § 240.21F-4(b)(4)(i-ii) and (iii)(C).

[7] *Adopting Release*, at 56.

[8] SEC Rule 21F-4(b)(4)(i-ii), 17 C.F.R. § 240.21F-4(b)(4)(i-ii)(2011).

[9] *Adopting Release*, *supra* note 1, at 60.

  SRLR ISSN 0037-0665

A. 'When permitted by § 205.3(d)(2).' Section 205.3(d)(2) of the standards of professional conduct for attorneys was issued by the SEC in 2003, pursuant to Section 307 of the Sarbanes-Oxley Act of 2002 (''SOX'').[10] Congress passed SOX in the wake of Enron and WorldCom, to provide greater protection for investors by improving corporate governance and increasing the reliability of financial reporting. Much of the Senate's consideration of SOX focused on the perceived shortcomings of outside auditors as gatekeepers. Senator Michael Enzi, the Senate's lone accountant, observed ''there ought to be some kind of an ethical standard put in place for the attorneys as well. . . . Maybe it could be called the 'smell test.' If something smells wrong, somebody who can do something to fix it ought to be told.''[11] Senator Enzi, in conjunction with Senator John Edwards, offered an amendment that was adopted and included in SOX as Section 307. Senator Edwards explained the purpose of their amendment:

> One of the most critical responsibilities that those lawyers have is, when they see something occurring or about to occur that violates the law, breaks the law, they must act as an advocate for the shareholders, for the company itself, for the investors. . . .They know the law and their responsibility is to do something about it if they see the law being broken or about to be broken.
>
> The amendment I am supporting would not require the attorneys to report violations to the SEC, only to corporate legal counsel or the [chief executive officer], and ultimately, to the board of directors.[12]

Section 307 directed the SEC to issue rules ''setting forth minimum standards of professional conduct for attorneys appearing and practicing before the Commission in any way in the representation of issuers'' including a rule requiring a covered attorney to ''report evidence of a material violation of securities law or breach of fiduciary duty or similar violation by the company or any agent thereof'' to the issuer's chief legal counsel or the CEO or both and, if an appropriate response is not received, to report the evidence to a committee of independent directors or to the full board. That directive led the SEC to issue Part 205.

Section 205 ''supplement[s] applicable standards of any jurisdiction where an attorney is admitted or practices.''[13] When a state rule addresses a subject not covered by § 205, the applicable state rule governs the conduct of lawyers licensed by that state. Where § 205 and a state rule impose conflicting obligations, the SEC states that § 205 ''shall govern'' unless the state rule ''impose[s] additional obligations on an attorney not inconsistent with the application of this part.''[14] For example, Section 205.3(b)(1) and many state rules identify when a lawyer for an organization has a duty to act. Section 205.3(b)(1) triggers a lawyer's duty when the lawyer becomes aware of *credible evidence* that it is ''reasonably likely that a material violation has occurred, is ongoing, or is about to occur.''[15] Many state rules require a lawyer to act when the lawyer *knows* of a violation of law that is likely to result in substantial injury to the organization.[16] Section 205.3(b)(3) *requires* a lawyer to report credible evidence of a material violation ''up the ladder'' if the lawyer reasonably believes that an appropriate and timely response has not been provided to the initial report.[17] Many state rules require a lawyer who knows of a violation of law *to proceed as reasonably necessary* in the best interest of the organization but do not necessarily impose a duty to report up the ladder.[18] In the SEC's view, the thresholds in Section 205.3(b)(1) and (3) establish when a lawyer's duty to report occurs and when a lawyer must report ''up the ladder,'' even if the circumstances would not trigger a duty to report or a duty to report ''up the ladder'' under applicable state rules.

In the event a covered lawyer determines that appropriate action has not been taken to address the ''credible evidence'' of a ''material violation,'' Section 205.3(d)(2) allows, but does not require, the lawyer to disclose client information to the SEC without client consent when the lawyer reasonably believes necessary:

> (i) To prevent the [client] from committing a material violation that is likely to cause substantial injury to the financial interest or property of the [client] or investors;
>
> (ii) To prevent the [client], in a Commission investigation or administrative proceeding from committing perjury, proscribed in 18 U.S.C. 1621; suborning perjury, proscribed in 18 U.S.C. 1622; or committing any act proscribed in 18 U.S.C. 1001 that is likely to perpetuate a fraud upon the Commission; or
>
> (iii) To rectify the consequences of a material violation by the [client] that caused, or may cause, substantial injury to the financial interest or property of the [client] or investors in the furtherance of which the attorney's services were used. [19]

In the hypothetical that opened this article, the lawyer would be authorized by § 205.3(d)(2)(i) to report to

---

[10] *See* Implementation of Standards of Professional Conduct for Attorneys (Final Rule), Securities Act Release No. 33-8185, Exchange Act Release No. 34-47276 (Jan. 29, 2003), *available at* http://www.sec.gov/rules/final/33-8185.htm.

[11] 148 Cong. Rec. S654-55 (daily ed. July 10, 2002) (statement of Sen. Enzi). He elaborated on that concept: ''lawyers who are responsible for the corporations' securities compliance work to report to the board of directors'' if senior management fails to address an identified violation of law.

[12] 148 Cong. Rec. S6551-52 (daily ed. July 10, 2002) (statement of Sen. Edwards); 148 Cong. Rec. S6554 (daily ed. July 10, 2002) (statement of Sen. Enzi).

[13] 17 C.F.R. § 205.1.

[14] 17 C.F.R. § 205.1. *See also* Implementation of Standards of Professional Conduct for Attorneys (Final Rule), Securities Act Release No. 33-8185, Exchange Act Release No. 34-47276 (Jan 29, 2003) (stating that Part 205 will ''prevail over any conflicting or inconsistent laws of a state or other United States jurisdiction in which an attorney is admitted or practices''), *available at* http://www.sec.gov/rules/final/33-8185.htm.

[15] For purposes of Part 205, ''material violation'' means ''a material violation of an applicable United States federal or state securities law, a material breach of fiduciary duty arising under United States federal or state law, or a similar material violation of any United States federal or state law.'' 17 CFR § 205.2(i).

[16] *See*, *e.g.*, Arizona, Arkansas, Idaho, Indiana, Kentucky. The SEC expressly rejected the threshold imposed by state rules as ''too high.'' It explained internal reporting triggered by ''credible evidence'' of a ''material violation'' would ''encourage the reporting of evidence of material violations.'' *Adopting Release*, *supra* note 1, at text accompanying nn. 49-50, http://www.sec.gov/rules/final/33-8185.htm.

[17] 17 C.F.R. 205.3(b)(2).

[18] *See e.g.*, Arizona, Arkansas, Idaho, Indiana, Kentucky.

[19] 17 C.F.R. § 205.3(d).

the SEC the concerns previously raised to the audit committee, to the extent he or she believed such a report would be reasonably necessary to prevent the company from committing a material violation likely to harm the company or its shareholders. Now that § 205.3(d)(2) has been incorporated into the SEC's Whistleblower Rules, that same lawyer could be eligible for a whistleblower bounty for reporting the company's confidential information to the SEC.[20]

B. 'When permitted by applicable state attorney conduct rules.' As the U.S. Supreme Court has observed, ''[s]ince the founding of the Republic, the licensing and regulation of lawyers has been left exclusively to the States and the District of Columbia within their respective jurisdictions. The States prescribe the qualifications for admission to practice and the standards of professional conduct. They are also responsible for the discipline of lawyers.''[21] A state-issued law license confers a right to practice and also imposes significant responsibilities (and potential liabilities). Those responsibilities are driven by three core duties: the duty of undivided, unconflicted loyalty to the client; the duty to protect client information; and the duty of candor to the court.

As codified in all state rules, a lawyer must refrain from knowingly revealing information relating to the representation of a client unless the client consents, and that obligation continues after the termination of the client-lawyer relationship. Virtually every state, however, recognizes at least one exception to this duty based on the state's balance of two competing public interests: the interest in requiring lawyers to preserve the confidentiality of information relating to the representation of their client; and the interest in preventing harm to third persons likely to result from a client's illegal and/or fraudulent acts or mitigating the harm caused by such acts where the lawyer's services were used. The scope of exceptions among the states reflect different weighting of each of these competing interests. But no state has weighted those interests to authorize a lawyer to disclose client information to a third party, absent client consent, for the purpose of obtaining a personal benefit, like a SEC a whistleblower bounty.[22]

1. Third Party Disclosure in the Leading "Whistleblower States." The rules of professional conduct adopted by each of the four states with the largest number of SEC whistleblower complaints for fiscal year 2012 and FY 2013—New York, California, Texas and Florida[23]—authorize disclosure of client information in narrower circumstances than those authorized by § 205.3(d)(2).

- New York Rule of Professional Conduct (''NYRPC'') 1.6(b)(2) only authorizes a lawyer to disclose client confidences without client consent as the ''lawyer reasonably believes necessary to prevent the client from committing a crime'' and prohibits disclosure where the client's actions constitute civil fraud or material violations of a civil statute. NYRCP 1.6(a) forbids disclosure to rectify the consequences of any violation of law, whether civil or criminal.[24] The Committee on Professional Ethics of the New York County Lawyers' Association recently opined that ''there are few circumstances, if any, in which, in the Committee's view, it would be reasonably necessary within the meaning of [NYRPC] 1.6(b) for a lawyer to pursue the steps necessary to collect a bounty as a reward for revealing confidential material.''[25]
- Texas Rule of Professional Conduct (''TRPC'') 1.05(c)(7) authorizes permissive disclosure ''to prevent the client from committing a criminal or fraudulent act,'' a narrower formulation than Part 205.3(d)(i), which permits disclosure to prevent a material violation of a civil statute that does not involve fraud.[26] TRPC 1.05(c)(8), which authorizes permissive disclosure of a client's past ''criminal or fraudulent act in the commission of which the lawyer's services had been used'' to rectify the consequences is narrower in scope than Part 205.3(d)(iii), which permits disclosure to address the ''consequences of a material violation'' of state or federal law.
- Florida Rule of Professional Conduct (''FRPC'') 4-1.6(b)(1) requires a lawyer to reveal information relating to representation of a client ''to the extent the lawyer reasonably believes necessary to prevent a client

[20] *Adopting Release*, *supra* note 1, at 56.

[21] *Leis v. Flynt*, 439 U.S. 438, 442 (1979).

[22] To the extent some state rules permit any disclosure for the lawyer's personal benefit, such exceptions are typically limited to information necessary to establish a claim or defense in a controversy between the lawyer and the client.

[23] U.S. Securities and Exchange Commission, *Annual Report on the Dodd-Frank Whistleblower Program Fiscal Year 2013* (November 2013), Appendix C, *available at* http://www.sec.gov/about/offices/owb/annual-report-2013.pdf;

U.S. Securities and Exchange Commission, *Annual Report on the Dodd-Frank Whistleblower Program Fiscal Year 2012* (November 2012), Appendix B, *available at* http://www.sec.gov/about/offices/owb/annual-report-2012.pdf.

[24] NYRPC 1.6(a), 1.6(b)(2). NYRCP 1.13(b) is significantly different from the initial duty to report set forth in Section 205.3(b)(1). Unlike Section 205.3(b)(1) which requires a lawyer to report ''credible evidence'' when the violation is ''more than a mere possibility, but it need not be more likely than not,'' (Adopting Release at text accompanying notes 49-50), the duty to act under NYRCP 1.13(b) is triggered when a lawyer for an organization knows of a violation of law. Once that threshold is met, NYRCP 1.13(b) tasks the lawyer with proceeding ''as is reasonably necessary in the best interest of the organization'' taking into account ''the scope and nature of the lawyer's representation, the responsibility in the organization and the apparent motivation of the person involved, the policies of the organization concerning such matters and any other relevant considerations.'' If the violations are not remedied internally, NYRPC 1.13(c) authorizes a lawyer to disclose client confidences to third parties without client consent ''only if permitted by Rule 1.6''—which limits disclosure to ''prevent a crime.''

[25] Formal Opinion 746, *Ethical Conflicts Caused by Lawyers as Whistleblowers under the Dodd-Frank Wall Street Reform Act of 2011*, Committee on Professional Ethics, N.Y. CNTY. LAWYERS' ASS'N, at 9 (Oct. 7, 2013) (''*Ethical Conflicts''*), https://www.nycla.org/siteFiles/Publications/Publications1647_0.pdf.

[26] Similar to NYRCP 1.13(b), TRPC 1.12(b) triggers a duty to act when the ''lawyer learns or knows'' of a violation of law. Texas does not have a mandatory ''up the ladder'' reporting requirement. TRPC1.12(b) requires a lawyer who ''learns or knows'' of a violation of law to ''take reasonable remedial actions.'' Pursuant to TRPC 1.12 (c), the actions can include ''up the ladder'' reporting. In the event the organization's highest authority ''persists in a course of action that is clearly violative of law or of a legal obligation to the organization and is likely to result in substantial injury to the organization,'' the lawyer's ability to disclosure client information to third parties is governed by TPRC 1.05. Comment 7, TRPC 1.12.

  SRLR ISSN 0037-0665

from committing a crime.'' FRPC 4-1.6(c)(1-5) contains none of the permissive disclosure exceptions in Part 205.3(d)(i) and (iii). And FRPC 4-1.6(a) forbids permissive disclosure of information relating to a client's material violation of a civil statute or to rectify the consequences of a material violation of any civil or criminal statute.[27]

■ California imposes a fiduciary duty on lawyers to maintain confidentiality by statute.[28] California Rule of Professional Conduct (''CRPC'') 3-100 authorizes permissive disclosure only where the lawyer ''reasonably believes the disclosure is necessary to prevent a criminal act that the member reasonably believes is likely to result in death of, or substantial bodily harm to, an individual,'' after the lawyer makes a good faith effort to dissuade the client from committing the criminal act.[29]

2. Third Party Disclosure Under Other State Rules. The relevant permissive and mandatory disclosure exceptions to a lawyer's duty to maintain the confidentiality of client information, as codified in the rules of professional conduct in the other 46 states and the District of Columbia are similarly nuanced.

Disclosure to prevent a crime likely to result in financial harm.

Most—but not all[30]—state rules contain an exception similar to one portion of § 205.3(d)(i): they authorize a lawyer to disclose client information to a third party, without client consent, to prevent commission of a crime that is likely (or reasonably certain) to result in substantial injury to the financial interest or property of another.[31] Some of these jurisdictions adopt the qualification used in American Bar Association Model Rule 1.6(b)(2) and require that the client must use the lawyer's services in connection with an intended crime before permissive disclosure is allowed.[32] A handful—like Florida—*require* lawyers to disclose client information to a third party to prevent commission of a crime that is likely (or reasonably certain) to result in substantial financial injury.[33]

Disclosure to prevent civil fraud.

Section 205.3(d)(i) also authorizes a lawyer to disclose client information to a third party, absent client consent, to prevent civil fraud that is likely (or reasonably certain) to result in substantial financial injury. Five states have adopted a similar exclusion.[34] Twenty-two states and the District of Columbia have adopted the qualification used in ABA Model Rule 1.6(b)(2): the client must use the lawyer's services in furtherance of the intended civil fraud.[35] Three states require lawyers to disclose client information to a third party to prevent commission of civil fraud that is likely (or reasonably certain) to result in substantial financial injury.[36] Twenty states, however, forbid lawyers from disclosing client information to third parties without consent to prevent the client's commission of civil fraud, regardless of the expected consequences.[37]

Disclosure to prevent material violations of non-fraud civil statutes.

Section 205.3(d)(i) authorizes a lawyer to disclose client information to a third party, absent client consent, to prevent the client from committing a ''material violation'' of a civil statute involving non-fraudulent conduct which is likely to cause substantial financial injury. We found no state rules that permits such disclosure.

Disclosure to rectify past misconduct.

Section 205.3(d)(iii) authorizes a lawyer to disclose client information to third parties to ''rectify the consequences of a material violation [that occurred in the past] . . . that caused . . . substantial injury . . . in the furtherance of which the attorney's services were used.''

---

[27] FRPC 4-1.6(a). Florida, like New York and Texas, requires a lawyer for an organization to know of a violation of law before the duty to act is triggered. FRPC 4-1.13(b). Once that standard has been met, the ''lawyer shall proceed as is reasonably necessary in the best interest of the organization'' which can include ''up the ladder'' reporting. FRPC 4-1.13(b). In the event the violation is not remediated, the lawyer's authority to disclose client information to a third party is limited by FRPC 4-1.6. See Comment 2, FRPC 1.13.

[28] CRPC 3-100A; California Business and Professions Code § 6068(e) (attorneys are obligated to ''maintain inviolate the confidence, and at every peril to himself or herself to preserve the secrets, of his or her client'').

[29] CRPC 3-600(B),(C). California has adopted the same trigger as New York, Texas and Florida: a lawyer must know of a violation of law before the lawyer is required to act. CRPC 3-600(B). When that duty is activated, the lawyer may report ''up the ladder.'' In the event that the violation of law is not addressed by the organization, the CRPC limits the lawyer's options to withdrawal. CRPC 3-600(C). The Corporations Committee of the Business Law Section and Committee on Professional Responsibility and Conduct of the State Bar of California opined that the exceptions in Part 205.3(d) appear to conflict with California law requiring attorneys to maintain client confidences. *See* Ethics Alert: The New SEC Attorney Conduct Rules v. California's Duty of Confidentiality (Spring 2004), http://ethics.calbar.ca.gov/LinkClick.aspx?fileticket=7xTdfWYEC3k%3D&tabid=834.

[30] Seven jurisdictions forbid disclosure of an intended crime: Alabama, California, Kentucky, Missouri, Montana, Rhode Island, and South Dakota.

[31] *E.g.*, Arkansas, Colorado, Connecticut, Georgia, Hawaii, Idaho, Kansas, Massachusetts, Michigan, Nebraska, New Hampshire, New Mexico, Ohio, Oklahoma, Oregon, Pennsylvania, Tennessee (and must withdraw), Washington, West Virginia, and Wyoming. Some states, like New York and Texas, permit disclosure to prevent a crime, regardless of the injury that the crime may cause.

[32] *E.g.*, Alaska, Arizona, Delaware, District of Columbia, Illinois, Indiana, Iowa, Louisiana, Maine, Maryland, Minnesota, Mississippi, Nevada, North Carolina, North Dakota, South Carolina and Utah.

[33] *E.g.*, Florida, New Jersey, Vermont, Virginia and Wisconsin. The latter three mandate disclosure to prevent a client from committing a crime.

The SEC has explicitly recognized that those obligations trump the permissive disclosures authorized in Part 205. *See* Section 205.1.

[34] *E.g.*, Connecticut, Hawaii, Massachusetts, Nebraska, and Texas.

[35] *E.g.*, Alaska, Arizona, Arkansas, Colorado, Delaware, District of Columbia, Illinois, Indiana, Iowa, Louisiana, Maine, Maryland, Minnesota, Mississippi, Nevada, North Carolina, North Dakota, Oklahoma, Pennsylvania, South Carolina, Tennessee (and must withdraw), Utah, and Washington.

[36] *E.g.*, New Jersey, Vermont, and Wisconsin. The latter two mandate disclosure to prevent a client from committing a criminal or fraudulent act that is reasonably certain to result in substantial financial injury to a third party where the client has used the lawyer's services. The SEC has explicitly recognized that those obligations trump the permissive disclosures authorized in Part 205. *See* Section 205.1.

[37] *E.g.*, Alabama, California, Florida, Georgia, Idaho, Kansas, Kentucky, Michigan, Missouri, Montana, New Hampshire, New Mexico, New York, Ohio, Oregon, Rhode Island, South Dakota. Virginia, West Virginia, and Wyoming.

	Rule permits third-party disclosure to:				
	Prevent a crime likely to result in financial harm	Prevent civil fraud	Prevent a material violation involving non-fraudulent conduct	Rectify consequences of a criminal or fraudulent act*	Rectify consequences of a material violation involving non-fraudulent conduct*
SEC Rule 205.3(d)	✓	✓	✓	✓	✓
Texas Rule 1.05	✓	✓		✓	
New York Rule 1.6	✓				
Florida Rule 4-1.6	✓^				
California Rule 3-100					

* Disclosure permitted to rectify past misconduct where the attorney's services were used in furtherance of the misconduct
^ Disclosure is required

This exception is directed at disclosing past conduct that caused injury. A majority of states permit a lawyer to disclose client information to third parties without consent to remedy substantial financial injury from a client's past crime or fraud, although the formulation differs among the states.[38] A significant minority of jurisdictions—15—forbid any disclosure to address injury from past conduct, whether civil or criminal.[39] We found no state rules authorizing a lawyer to disclose client information to rectify financial injuries resulting from a client's past material violation of a civil statute involving non-fraudulent conduct.

The differences between the § 205.3(d)(2) exceptions and exceptions in a state's confidentiality rules may be further complicated when a covered lawyer is licensed in more than one state, when a lawyer's conduct involves significant contacts with more than one state, and when the potentially applicable state rules have different exceptions for permissive disclosures.

C. 'Otherwise.' The SEC's Adopting Release provides no explanation of the facts that would trigger the ''otherwise'' exclusion or of the circumstances that might give rise to this exclusion that would not otherwise be included within Part 205 or the applicable state rules of professional conduct.

II. The SEC's Assertion of Preemption: Has Congress Delegated Authority in Dodd-Frank to the SEC to Immunize Lawyers from Violations of State Confidentiality Rules When They Disclose Client Information to the SEC for Their Own Financial Benefit?

In our opening hypothetical, the lawyer reasonably believes that issuance of the 10-K without further clarification could amount to a non-fraud based civil violation of a federal securities law that will likely cause substantial financial injury to investors. In these circumstances, disclosure of client information to the SEC would be permitted under Section 205.3(d)(2) but not

[38] Virtually all states that permit disclosure under these circumstances require that the client used the lawyer's services to commit the crime or fraud. *E.g.*, Alaska, Arizona, Arkansas, Colorado, Connecticut, Delaware, District of Columbia, Hawaii, Idaho, Illinois, Indiana, Iowa, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, Nevada, New Jersey, North Carolina, North Dakota, Ohio, Oklahoma, Pennsylvania, South Carolina, South Dakota, Tennessee, Texas, Utah, Washington and Wisconsin.

[39] Alabama, California, Florida, Georgia, Kansas, Kentucky, Missouri, Montana, Nebraska, New Hampshire, New Mexico, Oregon, Rhode Island, West Virginia and Wyoming.

  SRLR ISSN 0037-0665

under applicable state rules (unless the client provided informed consent).

When it promulgated Part 205, the SEC explained that preemption of conflicting state ethics rules was needed to protect ''the public interest where an issuer seeks to commit a material violation that will materially damage investors, seeks to perpetrate a fraud upon the Commission in enforcement proceedings, or has used the attorney's services to commit a material violation.''[40] While much ink has been spilled attacking and defending the SEC's claim that Part 205 preempts conflicting state rules,[41] no court has addressed the issue, perhaps because few, if any, lawyers have relied on it to disclose client information to the SEC.[42]

Whatever the merits of the SEC's claim, the preemption analysis necessarily changes with the incorporation of the § 205.3(d)(2) exceptions into the SEC whistleblower rules because the purpose for the disclosure exceptions is different. The SEC's rules incentivize lawyers to become award-seeking SEC whistleblowers by disclosing client information without consent under § 205.3(d)(2) for the lawyer's personal benefit. Where, as here, a federal administrative agency makes an ''assertion of preemptive power to displace state or local regulatory authority,'' courts require ''an unmistakably clear statement from Congress before interpreting federal law to displace state and local power.''[43] Congress expressed a clear intent to preempt inconsistent state law in a number of Dodd-Frank provisions. For example, Section 1041 provides that the Consumer Financial Protection Act in Title X of Dodd-Frank preempts conflicting state laws which are deemed inconsistent by the Bureau of Consumer Financial Protection and provides a structure to identify and resolve the conflicts. Section 1044 establishes a new regime for national bank federal preemption of state consumer financial laws and, among other things, identifies three categories of state consumer financial laws that are preempted and explains the process by which the Office of the Comptroller of the Currency will make preemption determinations. In contrast, Section 922—the SEC Whistleblower Program—contains no explicit reference to preemption.

Preemption can also be found where Congress intended the federal legislation to ''occupy the field'' with respect to that subject. Congressional intent to occupy the field can be inferred from a statute's legislative history, its comprehensiveness and a federal interest in dominating the subject matter.[44] The Supreme Court has instructed that courts must apply a presumption against field preemption in regard to subject matters ''traditionally regarded as properly within the scope of state superintendence.''[45] Because states have long used their police powers to regulate lawyers and because the legislative history of Section 922 contains no intent by Congress to occupy a field traditionally governed by state law, a finding of implied field preemption seems unlikely.

Absent express statutory preemption or implied field preemption, the source of the SEC's authority to preempt conflicting state rules and laws with the whistleblower rules can only be found if Congress intended to delegate such authority to it.[46] For a claim of implied conflict preemption to succeed, a two-part test must be satisfied: (1) whether the federal agency intended to preempt state law when it promulgated the regulation; and (2) whether its regulation is a valid exercise of congressionally-delegated authority.[47] By incorporating § 205.3(d)(2) into Rule 21F-4(b)(4)(i), the SEC made clear that it intended Rule 21F-4(b)(4)(1) to preempt conflicting state rules of professional conduct. The Supreme Court has repeatedly emphasized that, ''[i]n areas of traditional state regulation, [it] assume[s] that a federal statute has not supplanted state law unless Congress has made such an intention clear and manifest.''[48] Here, there is no evidence in the legislative history of Dodd-Frank or in the language of Section 922 of Congress' ''clear and manifest'' intent to delegate to the SEC authority to adopt a rule preempting conflicting state rules in order to incentivize lawyers to turn on their clients and disclose client information to the SEC for the purpose of obtaining a whistleblower reward.

As of this writing, no federal court has ruled on whether a lawyer who discloses client information to the SEC without consent, pursuant to the § 205.3(d)(2) exception in SEC Rule 21F-4(b)(4)(i), in an effort to obtain a SEC whistleblower bounty is immunized from liability in private actions or in state disciplinary proceedings if such disclosures are prohibited under applicable state rules of professional conduct. A similar issue has arisen in False Claims Act *qui tam* cases and the few federal courts to address the issue have held that ''[n]othing in the False Claims Act evinces a clear legislative intent to preempt state statutes and rules that

---

[40] Implementation of Standards of Professional Conduct for Attorneys, Securities Act Release No. 33-8185, Exchange Act Release No. 34-47276, at text accompanying note 112 (Jan 29, 2003), http://www.sec.gov/rules/final/33-8185.htm.

[41] *Compare*, for example, Roger Cramton, George Cohen & Susan Koniak, *Legal and Ethical Duties of Lawyers After Sarbanes Oxley*, 49 VILL. L. REV. 725, 782 (2004) (arguing implied preemption), *with* Corporations Committee of the Business Law Section of the California State Bar, *Conflicting Currents: The Obligation to Maintain Inviolate Client Confidences and the New SEC Attorney Conduct Rules*, 32 PEPP. L. REV. 89 (2004) (arguing preemption of inconsistent state law appears to exceed the grant of authority from Congress to the SEC in Section 307). For a discussion of the conflicting positions taken by the Washington state bar association and the SEC's General Counsel, *see* C. Evan Stewart, *The Pit, the Pendulum, and the Legal Profession: Where Do We Stand After Five Years of Sarbanes-Oxley?*, 40 BLOOMBERG BNA SEC. REG. & L. REP. 247 (Feb. 18, 2008).

[42] Stephen Joyce, *SEC Enforcement Unit Concerned Defense Lawyers May Be Obstructing Probes*, BLOOMBERG BNA DAILY REP. FOR EXECUTIVES (November 12, 2013) (reporting remarks by SEC Associate General Counsel Richard M. Humes), available at http://dailyreport.bna.com/drpt/7010/split_display.adp?fedfid=38116990&vname=dernotallissues&wsn=498520500&searchid=21532671&doctypeid=1&type=date&mode=doc&split=0&scm=7010&pg=0.

[43] *Gregory v. Ashcroft*, 501 U.S. 452, 458 (1991). See also *ABA v. FTC*, 430 F.3d 457, 466 (D.C. Cir. 2005) (holding that Congress did not delegate to the FTC the authority to regulate the practice of law under Gramm-Leach-Bliley).

[44] *English v. Gen. Elec. Co*., 496 U.S. 72, 78–79 (1990). See also *Cipollone v. Liggett Grp., Inc.*, 505 U.S. 504, 516 (1992).

[45] *Fla. Lime & Avocado Growers Inc. v. Pauli,* 373 U.S. 132, 144 (1963).

[46] *E.g*., *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947).

[47] *City of New York v. FCC*, 486 U.S. 57, 63-64 (1988).

[48] *Bates v. Dow Agrosiences LLC*, 544 U.S. 431, 449 (2005) (internal quotations omitted). *See also Cipollone*, 505 U.S. at 516 (same).

regulate an attorney's disclosure of client confidences.''[49]

Finding the False Claims Act does not preempt state ethics rules protecting client information, courts have examined exceptions to the applicable state rule and concluded that they did not permit the disclosures made by the attorney-relator. The recent decision by the U.S. Court of Appeals for the Second Circuit in *United States ex rel. Fair Laboratory Practices Associates v. Quest Diagnostics, Inc.* is instructive.[50] There, the attorney-relator maintained that his disclosures of confidential client information to third parties fell within the applicable New York rule permitting disclosure of information necessary to reveal ''[t]he intention of a client to commit a crime and the information necessary to prevent the crime. . . .''[51] The district court found that the attorney-relator could have reasonably believed that the defendants intended to commit a crime when the *qui tam* action was filed but that his disclosures of client information went beyond those reasonably necessary to prevent a crime in violation of his ethical obligations under the New York rules.[52] It determined that the appropriate remedy for this violation was disqualification of the attorney-relator, his partners, and their counsel from the *qui tam* action and any subsequent action involving the same facts. The Second Circuit affirmed both the district court's factual findings that the disclosure by the attorney-relator of client information was greater than reasonably necessary to prevent any alleged ongoing crime as well as the disqualification remedy.

III. Lawyers as Whistleblowers: Do Other State Conduct Rules Apply?

SEC Associate General Counsel Richard Humes recently cautioned that a lawyer who seeks to rely on § 205.3(d)(2) exception in SEC Rule 21F-4(b)(4)(i) to voluntarily report client information to the SEC in order to obtain a whistleblower award may be subject to state bar disciplinary actions for violations of state confidentiality rules, may risk being sued by the affected client and may lose future business from potential clients who fear the lawyer will again divulge client information to the SEC.[53] Although many lawyers facing the circumstances in the opening hypothetical would likely be uncomfortable in relying solely on the § 205.3(d)(2) exception because of the possible reputational risks and financial costs, the SEC's recent award of a $14 million whistleblower bounty may provide sufficient incentive to some covered lawyers to take such risks.

While the preemptive effect of SEC Rule 21F-4(b)(4)(i) on conflicting state confidentiality rules is a question of substantive law to be decided by the courts, that Rule does not authorize any lawyer to violate any other obligation imposed by state statutes and professional conduct rules. For example, every state has adopted rules codifying a lawyer's duties of undivided and unconflicted loyalty to current clients and duties to former clients. Because § 205.3(d)(2) and Rule 21F-4(b)(4) contain no conflicts of interest provisions, a lawyer contemplating a whistleblower complaint must comply with the rules of the licensing state on conflicts of interest. Although the formulation of the conflicts rules vary among the states, the same fundamental principle underlies all state conflicts rules involving current clients: absent full disclosure and informed client consent, a lawyer shall not represent a client if there is a significant risk that the lawyer's own interests, whether involving a purse string, heart string, or some other tie, will materially interfere with the lawyer's independent professional judgment on behalf of the client.[54]

---

[49] *United States ex rel. Fair Lab. Practices Assocs. v. Quest Diagnostics, Inc.*, 734 F.3d 154 (2d Cir. 2013), *affirming United States ex rel. Fair Lab. Practices Assocs. v. Quest Diagnostics, Inc.*, No. 05 Civ. 5393, 2011 BL 90888, at *5 (S.D.N.Y. Apr. 5, 2011). *See also United States ex rel. Doe v. X. Corp.*, 862 F. Supp. 1502, 1507 (E.D. Va. 1994) (after defendant settled with the government, court held that *qui tam* lawyer-relator was not entitled to statutory share of False Claims Act recovery on grounds that False Claims Act did not ''immunize a relator for actions taken in pursuance of a *qui tam* action that violate state law''); *Bury v. Cmty. Hosps. of Cent. Cal.*, No. F036667, 2002 BL 7464, at *4, 5 (Cal. Ct. App. May 8, 2002) (California appellate court affirmed the dismissal of a *qui tam* action under the state false claims act, patterned after the federal False Claims Act because the lawyer-relator was barred by state rules of conduct from disclosing confidential information to support the claim).

Indeed, a number of courts have been unwilling to permit non-attorney relators to use confidential information from employers to pursue False Claims Act *qui tam* actions where documents were improperly obtained under state law and have sanctioned relators' counsel for failing to report that their client had improperly taken such documents. *See, e.g., United States ex rel. Cafasso v. Gen. Dynamics C4 Sys., Inc.*, 637 F.3d 1047, 1061-62 (9th Cir. 2011) (holding that a duly executed confidentiality agreement enforceable under state law was not nullified by the False Claims Act and barring a former employee from using documents taken from a former employer, in violation of the confidentiality agreement, to support a *qui tam* action); *United States ex rel. Hartpence v. Kinetic Concepts, Inc.*, Case No. 08-01885 (C.D. Cal. Nov. 9, 2012) (Dkt. No. 125) (ordering relators, who regularly interacted with counsel for their former employer, to return hundreds of attorney-client communications improperly taken from former employer and barring use of those communications in the *qui tam* action); *United States ex rel. Hartpence v. Kinetic Concepts, Inc.*, Case No. 08-01885, 2013 WL 2278122, at *2 (C.D. Cal. May 20, 2013) (disqualifying relator's counsel on the ground that they knowingly and improperly used privileged documents in relators' pleadings); *United States ex rel. Frazier v. IASIS Healthcare Corp.*, Case No.: 2:05-cv-00766, 2012 BL 62403, at *14 (D. Ariz. Jan. 12, 2012) (disqualifying relator's counsel and ordering counsel to pay defendant's fees and costs where counsel was given documents by the relator that were marked as privileged communications of the defendant and counsel segregated those documents and did not review them but did not notify the court or return them to the defendant).

[50] *United States of America ex rel. Fair Lab. Practices Assocs. v. Quest Diagnostics, Inc.*, No. 05 Civ. 5393, 2011 BL 90888, at *5 (S.D.N.Y. Apr. 5, 2011).

[51] *Id.* at *9-10.

[52] *See id.* at *10.

[53] Stephen Joyce, *SEC Enforcement Unit Concerned Defense Lawyers May Be Obstructing Probes*, BLOOMBERG BNA DAILY REP. FOR EXECUTIVES (Nov. 12, 2013) (reporting remarks by SEC Associate General Counsel Richard M. Humes), *available at* http://dailyreport.bna.com/drpt/7010/split_display.adp?fedfid=38116990&vname=dernotallissues&wsn=498520500&searchid=21532671&doctypeid=1&type=date&mode=doc&split=0&scm=7010&pg=0.

[54] *E.g.*, NYRPC 1.7(a) (Absent consent, ''a lawyer shall not represent a client if a reasonable lawyer would conclude that either: (1) the representation will involve the lawyer in representing differing interests; or (2) there is a significant risk that

  SRLR ISSN 0037-0665

Determining whether a ''significant risk'' exists is not scientific. In a recent opinion, the Committee on Professional Ethics of the New York County Lawyers' Association drew a bright line: any possible whistleblower bounty in excess of $100,000 constitutes a significant risk that the ''lawyer's professional judgment [on behalf of a client] may be affected by the prospect of a monetary bounty.''[55] Notwithstanding the significant risk, the conflict may be waivable if the lawyer ''reasonably believes'' that he or she will be able to provide competent and diligent representation, makes full disclosure of the conflict and obtains informed consent from the client before the whistleblower complaint is filed, which seems highly improbable in the SEC whistleblower context. In certain circumstances, a conflict between the lawyer-whistleblower and the client may be unwaivable: the New York County Professional Ethics Committee's opinion suggests that a possible whistleblower bounty of $10 million may create an unwaivable conflict because it ''would tend to cloud lawyers' professional judgment, influencing lawyers to report out a violation regardless of their clients' interests.''[56]

Because lawyers owe duties to former clients, resigning from the representation would not cure the conflict. In a substantial number of states, the conflict rules forbid a lawyer from using or disclosing information learned during a representation to the disadvantage of the former client unless other state rules permit or require disclosure. Some case law suggests that a lawyer's duty to former clients is not limited solely to protecting the former client's confidences but includes a common law fiduciary duty of loyalty. For example, the California Supreme Court recently held that a lawyer's duty of loyalty and confidentiality survived the termination of the attorney-client relationship.[57] There, a lawyer who had represented a real estate venture in connection with its efforts to obtain approvals for a redevelopment project subsequently lent his personal support to a citizens' group opposed to the project after the representation ended. After the lawyer was sued by his former client for breach of fiduciary duty and breach of contract, the lawyer moved to dismiss on a number of grounds, including that a lawyer's fiduciary obligations to a former client were limited and only barred the lawyer from undertaking a representation for another client that was substantially related to the prior representation of the former client and is adverse to the former client or where the lawyer actually disclosed client information to the disadvantage of the former client. The California Supreme Court rejected that argument. It held that a lawyer's duties of loyalty and confidentiality to a former client extended to instances where the lawyer used client information to ''frame a course of action,'' even where the lawyer was ''not working on behalf of a new client, and even if none of the information [was] actually disclosed.''[58]

IV. When Secretkeepers Contemplate Whistleblower Bounties: What's an Issuer to Do?

Until the reach of SEC Rule 21-F4(b)(4)(i) is resolved by the courts, organizations subject to the Dodd-Frank whistleblower program should consider a number of strategies to reduce the risk that their lawyers will become award-seeking SEC whistleblowers.

At the beginning of the lawyers' employment, organizations might consider establishing written ground rules, in an employment contract or annual attestation, regarding up the ladder reporting, use or disclosure of information learned during the representation, com-

---

the lawyer's professional judgment on behalf of a client will be adversely affected by the lawyer's own financial, business, property or other personal interests.''); FRPC 4-1.7(a) (Absent client consent, a lawyer ''shall not represent a client if: (1) the representation of 1 client will be directly adverse to another client; or (2) there is a substantial risk that the representation of 1 or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.''); TRPC 1.06(b) (Absent client consent, a lawyer ''shall not represent a person if the representation of that person: (1) involves a substantially related matter in which that person's interests are materially and directly adverse to the interests of another client of the lawyer or the lawyers firm; or (2) reasonably appears to be or become adversely limited by the lawyers or law firm's responsibilities to another client or to a third person or by the lawyers or law firm's own interests.''); CRPC 3-310(B)(4) (Absent consent, ''A member shall not accept or continue representation of a client where . . . [t]he member has or had a legal, business, financial, or professional interest in the subject matter of the representation.'').

[55] Formal Opinion 746, *Ethical Conflicts Caused by Lawyers as Whistleblowers under the Dodd-Frank Wall Street Reform Act of 2011*, Committee on Professional Ethics, New York County Lawyers' Association, at 11 (October 7, 2013) (''*Ethical Conflicts*''), https://www.nycla.org/siteFiles/Publications/Publications1647_0.pdf. Under its Dodd-Frank whistleblower program, the SEC has made a total of six whistleblower awards, the most recent of which was more than $14 million to one whistleblower. *See* Press Release, SEC, SEC Awards More Than $14 Million to Whistleblower, (October 1, 2013), http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370539854258. According to Sean McKessy, Director of the SEC's Office of the Whistleblower, the SEC has ''some very interesting ongoing investigations'' launched by whistleblower complaints and ''given our historical recovery in these kinds of cases, [could] mean very big numbers.'' Sarah Lynch, ''Bigger Payouts Seen for U.S. financial market Whistleblowers,'' Reuters (October 1, 2013), http://www.reuters.com/article/2013/10/01/us-financial-regulation-whistleblowers-idUSBRE9901EY20131001.

[56] *Ethical Conflicts*, *supra* note 25, at 12. In two criminal cases, the Second Circuit found that the conflict between the lawyer's representation of a criminal defendant and the lawyer's self-interest was ''of such a serious nature that no rational defendant would knowingly and intelligently desire that attorney's representation.'' *United States v. Schwarz*, 283 F.3d 76, 95 (2d Cir. 2002) (where lawyer representing a defendant police officer charged with assaulting a suspect in custody was subsequently retained by the Police Benevolent Association to defend it in a civil action brought by the victim of the assault and received a $10 million retainer for the civil representation and defendant was apprised of the facts and consented to the conflict waiver, court held that the conflict was not waivable because the financial interests of the lawyer diverged from the defendant's interests). *See also United States v. Fulton*, 5 F.3d 605 (2d Cir. 1993) (where counsel for a defendant charged with conspiracy to possess and import heroin was reported to have personally participated in a related heroin importation, court held that the attorney's self-interest in avoiding criminal liability and damage to his reputation collided with the interests of the defendant and could not be waived).

[57] *Oasis West Realty, LLC v. Goldman*, 51 Cal. 4th 811, 825 (Cal. 2011)

[58] *Id*. at 823.

pensation by third parties, and retention and use of client documents. What particular ground rules or combination of ground rules can organizations consider adopting at the outset of an in-house lawyers' employment?

■ Consider requiring ''up the ladder'' reporting of credible evidence of material violations of law, fiduciary duty, or the organization's Code of Conduct, regardless of whether the lawyer is covered under Part 205 and regardless of whether the lawyer ''knows'' the material violation has occurred or is about to occur or whether the lawyer's services were used in connection with the violation;

■ Consider obligating the lawyer to report credible evidence of material violations of law, fiduciary duty, or the Code of Conduct to a committee of independent directors (or to the entire board) when the lawyer reasonably believes that he or she has not received appropriate response to the initial report, even where the lawyer is not covered under Part 205;

■ Require the lawyer not to use or disclose any information learned during the representation, absent informed client consent, even after the representation terminates, unless such information was in the public domain, or disclosure to a third party is required by court order, state or federal law or the applicable rules of the state in which the lawyer was licensed;

■ Consider requiring the lawyer to refrain from accepting any compensation or other payments from a third party in connection with his or her employment (unrelated to insurance payments) and specifying damages for breach of the term as the amount of the compensation or payments received plus fees and costs;

■ Where an organization's code of conduct or other compliance policies obligate employees to report compliance concerns internally, an annual certification could be sought that asks the lawyer to acknowledge those obligations; and

■ Establish terms addressing the lawyer's copying and retention of client documents.

The SEC views confidentiality agreements and confidentiality provisions in employee agreements with skepticism because of concerns that they can intimidate employees from contacting the SEC.[59] In the False Claims Act setting, some courts have exempted individual qui tam relators, who were not lawyers, from liability for violations of confidentiality and nondisclosure agreements, provided that the public disclosures to the U.S. government were tailored to the qui tam allegations.[60] Unlike lawyers, however, non-lawyer employees do not have a professionally mandated ethical duty to maintain the confidentiality of client information. As discussed earlier, the SEC has expressly recognized that open communications between an issuer client and its counsel promotes compliance with the securities laws, which is an important societal benefit. While no contractual provision can override a lawyer's mandatory disclosure obligations under state or federal law, parties should be able to agree by contract on the limits of a lawyer's ability to use and/or disclose information learned during the representation when disclosure is not required by law.

Should a lawyer make an internal report of compliance concerns or possible misconduct, the organization should respond with the same care and diligence as it would to a report made by a non-lawyer.[61] Among other things, that response could include:

■ Using the processes established in the organization's Code of Conduct or whistleblower policy to conduct a prompt and thorough review of the potential misconduct;

■ Reiterating to the reporting lawyer the organization's zero tolerance for retaliation and underscoring the organization's intent to address all concerns regarding retaliatory or discriminatory conduct;

■ Guarding against intemperate and/or unsupported employment decisions involving the reporting lawyer that may drive a costly retaliation claim;

■ Ensuring that the reporting lawyer is kept informed on the progress of the review and on its findings, where appropriate;

■ Reminding the lawyer, where appropriate, of any contractual duty of confidentiality and of applicable limits on permissive disclosure of client information to third parties; and

■ Communicating with the reporting lawyer once a final conclusion is reached to assure him or her that the reported concerns have been appropriately addressed.

V. Conclusion

In the Adopting Release for its whistleblower rules, the SEC recognized that the important benefit gained from consultations with counsel about compliance with the federal securities laws ''could be undermined if the

[59] *See, e.g., Susan Beck's Summary Judgment: SEC's Whistleblower Chief Disappointed in Questions from Corporate America*, The American Lawyer (Nov. 26, 2012). SEC Whistleblower Rule 21F-17(a) provides that no person may take any action to impede a whistleblower from communicating directly with the Commission about a possible securities law violation, including by enforcing or threatening to enforce a confidentiality agreement with respect to such communications.

[60] *See, e.g., United States ex rel. Head v. Kane Co.*, 668 F. Supp. 2d 146, 152 (D.D.C. 2009) (declining to enforce confidentiality agreement where qui tam relator provided a single email to the Government). *See also, E.A. Renfroe & Co. v. Moran*, 249 F. App'x 88, 90-92 (11th Cir. 2007) (acknowledging that non-disclosure provisions in employment agreements did not apply to 15,000 corporate documents provided to the Government). *But see, United States ex rel.Cafasso v. Gen. Dynamics C4 Sys., Inc.*, 637 F.3d 1047 (9th Cir. 2011) (public policy exception to enforcement of confidentiality agreement did not cover indiscriminate copying of approximately eleven gigabytes of data from company computers).

[61] We have written previously about tools that an organization covered by Dodd-Frank could consider to review internal reports. *See* William McLucas, Laura Wertheimer & Arian June, *Dispatches From the Whistleblower Front: Five Common Pitfalls For Companies to Avoid*, 45 Bloomberg BNA Sec. Reg. & L. Rep. 1345 (July 22, 2013); William McLucas, Laura Wertheimer & Arian June, *Preparing for the Deluge: How to Respond When Employees Speak Up and Report Possible Compliance Violations*, 44 Bloomberg BNA Sec. Reg. & L. Rep. 922 (May 7, 2012).

  SRLR ISSN 0037-0665

whistleblower award program created monetary incentives for counsel to disclose information about possible securities violations in violation of their ethical duties to maintain client confidentiality.''[62]

However, the § 205.3(d)(2) exceptions in SEC Rule 21F-4(b) may incentivize lawyers to use or disclose client information to the SEC for their own financial benefit when such use or disclosure would be prohibited by applicable state confidentiality rule(s). We have proposed a number of strategies for organizations covered by Dodd-Frank to consider to contain the risk that their lawyers will morph into bounty hunters. While these strategies may not eliminate the risk, they can establish ground rules that establish the responsibilities of the organization's lawyers to appropriately report irregularities and concerns internally while protecting the confidentiality of the organization's information.

[62] *Adopting Release*, *supra* note 1, at 56.