Bloomberg BNA

Securities Regulation & Law Report™

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ENFORCEMENT

SEC Enforcement Developments: Renewed Focus on Lawyers

BY WILLIAM MCLUCAS, DOUGLAS DAVISON, AND MICHAEL LAMSON

Introduction

The Securities and Exchange Commission Enforcement Division staff has a long history of scrutinizing lawyers' conduct during its investigations. This scrutiny has tended to be cyclical—from the "access theory" that the staff favored during the 1970s, to emphasizing a lawyer's role as gatekeeper following the 2002 Sarbanes-Oxley Act. There are times when the SEC's vigor in investigating the role of professionals in its inquiries poses a serious potential risk for the lawyers who practice before the agency.

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It appears that we are amidst another cycle:

- At the SEC Speaks Conference held in February 2013, Enforcement Co-Director George Canellos and other Enforcement officials touted the staff's focus on corporate gatekeepers—including lawyers—as a key method to root out fraud.[1]

- In May 2013, Commissioner Daniel Gallagher noted in a speech that the SEC would hold individuals accountable for material misstatements or omissions made in connection with municipal securities transactions, a field in which lawyers advise municipalities regarding public disclosure obligations.[2]

- In July 2013, the SEC announced the formation of the Financial Reporting and Audit Task Force dedicated

[1] Peter Rawlings, *Canellos: SEC Targeting Gatekeeper Negligence*, COMPLIANCE REPORTER, Feb. 25, 2013. More recently, the SEC announced in a press release that its effort to focus on auditors who "fail to carry out their duties and responsibilities consistent with professional standards" had been internally designated as "Operation Broken Gate." *See* Press Release, SEC, *SEC Charges Three Auditors in Continuing Crackdown on Violations or Failures By Gatekeepers* (Sept. 30, 2013), http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370539850572.

[2] Daniel Gallagher, SEC Comm'r, Remarks at the 45th Annual Rocky Mountain Securities Conference (May 10, 2013), http://www.sec.gov/News/Speech/Detail/Speech/1365171515568.

to detecting fraudulent or improper financial reporting. We expect that the role of counsel in drafting periodic and other reports will likewise receive scrutiny.[3]

■ In a recent speech entitled ''Deploying the Full Enforcement Arsenal,'' SEC Chairman Mary Jo White said that in a ''subtle shift'' of Enforcement priorities, she had directed the staff to assess first in investigations whether individuals could be charged before looking to bring a case against an entity.[4] She also said that if the SEC cannot prove intentional fraud, it will bring actions premised on negligent conduct. In addition, more recently, Chairman White said that the SEC has adopted a ''tough cop'' approach, aiming to be ''everywhere, pursuing all types of violations . . . , big and small.''[5] She referred to the ''broken windows'' strategy emphasized in the 1990s by then-New York City Mayor Rudy Giuliani, intended to make clear that no violation was too small to be uncovered and punished. Chairman White reiterated the SEC's focus on gatekeepers in the financial system, and cautioned that the SEC ''will not be looking to charge a gatekeeper that did her job by asking the hard questions, demanding answers, looking for red flags and raising her hand.''

We believe that these statements, taken together with other developments discussed below, suggest that the staff will increasingly investigate and scrutinize the role of counsel. A critical question is whether the SEC will indeed follow its longstanding precedent in assessing the conduct of lawyers, which generally holds that lawyers are not liable for advice given in good faith and with a reasonable basis.[6] As a practical matter, practitioners and their clients should be mindful that counsel's advice may well come under intense scrutiny in the course of SEC investigations, and that possibility, in and of itself, poses both serious and complex issues for the private bar and the SEC.[7]

This article discusses certain aspects of both the history and renewed focus on lawyers who become subjects of SEC investigations and actions. We focus first on the important developments of the Enforcement Division's scrutiny of lawyers, including the SEC's specific authority to police the behavior of those who practice before it under Commission Rule of Practice 102(e) and its predecessor Rule 2(e),[8] as well as the background of the SEC's sometimes tense relationship with the private bar in connection with its use of its broad law enforcement powers. We will next discuss recent developments that have increased the risks to lawyers practicing before the Commission more than ever before. Finally, we then address the potential consequences and provide practical tips that clients and practitioners should consider in navigating the current SEC enforcement environment.

Significant Precedent and Policies Concerning SEC Actions Involving Lawyers

Looking back at the history of the Enforcement Division, several key developments related to the staff's scrutiny of lawyer conduct are particularly significant.

1. Access Theory

During the 1970s, Enforcement Director Stanley Sporkin developed and utilized the ''access theory'' of enforcement. Citing the SEC's perennial problem of limited personnel and resources to police the securities markets, Sporkin determined that rather than trying to catch every wrongdoer, that staff would focus on those who were critical to market participants gaining ''access'' to the capital markets, such as lawyers, accountants, underwriters, and securities market professionals. Sporkin believed that this focus on access would yield far more effective results. This effort and in particular the focus on lawyers, resulted in the strengthening of the compliance functions and legal departments generally in the private sector to ensure that their regulated entities and public companies did not violate the securities laws.[9]

2. Carter & Johnson: No Discipline for Reasoned but Wrong Legal Advice

The Commission's general approach to bringing disciplinary proceedings against lawyers under its Rules of

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[3] Press Release, SEC, *SEC Announces Enforcement Initiatives to Combat Financial Reporting and Microcap Fraud and Enhance Risk Analysis* (July 2, 2013), http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171624975. Indeed, Enforcement Co-Director Andrew Ceresney recently explained that the Task Force, comprised of lawyers and accountants, would be focused on accounting issues related to reserves, revenue recognition, and the role of audit committees, areas in which counsel plays a prominent role in providing advice to management and drafting public disclosures. *See* Andrew Ceresney, SEC Enforcement Co-Dir., Remarks at American Law Institute Continuing Legal Education (Sept. 19, 2013), http://www.sec.gov/News/Speech/Detail/Speech/1370539845772.

[4] Mary Jo White, SEC Chairman, Remarks at the Council of Institutional Investors Fall Conference (Sept. 26, 2013), http://www.sec.gov/News/Speech/Detail/Speech/1370539841202.

[5] Mary Jo White, SEC Chairman, Remarks at the Securities Enforcement Forum (Oct. 9, 2013), http://www.sec.gov/News/Speech/Detail/Speech/1370539872100.

[6] Giovanni P. Prezioso, SEC Gen. Counsel, Remarks before the Spring Meeting of the Association of General Counsel (Apr. 28, 2005), http://www.sec.gov/news/speech/spch042805gpp.htm (''[T]he Commission ordinarily will not sanction lawyers under the securities laws merely for giving bad advice, even if that advice is negligent and perhaps worse.'').

[7] The SEC's first settled action under the new policy of requiring admissions in certain settlements – the highly publicized settlement with Philip Falcone and his hedge fund, Harbinger Capital Partners – is a recent example of the SEC's focus on counsel's communications and their role in an enforcement action. In that matter, the SEC publicly outlined in court filings the role that outside counsel played in advising Falcone on a strategy to pay his personal tax obligations via a loan transaction. Press Release, SEC, *Court Enters Final Judgment by Consent Against SEC Defendants Philip A. Falcone, Harbinger Capital Partners Offshore Manager, L.L.C., Harbinger Capital Partners Special Situations Gp, L.L.C., and Harbinger Capital Partners LLC*, Litig. Rel. No. 22831A (Oct. 2, 2013).

[8] Rule 102(e) permits the Commission to censure, suspend, or disbar any professional that it finds, after opportunity for hearing: (1) to not possess the requisite qualifications to represent others; (2) to be lacking in character or integrity or to have engaged in unethical or improper professional conduct; or (3) to have willfully violated or willfully aided and abetted the violation of the federal securities laws or the rules and regulations thereunder. 17 C.F.R. § 201.102(e)(1) (2013).

[9] *See* Interview by Irving Pollack with Stanley Sporkin, in Washington, DC (Sept. 23, 2003), http://3197d6d14b5f19f2f440-5e13d29c4c016cf96cbbfd197c579b45.r81.cf1.rackcdn.com/collection/oral-histories/sporkin092303Transcript.pdf.

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Practice is to not sanction lawyers who provide reasoned legal advice that in hindsight turned out to be wrong. This approach is embodied in the Commission's seminal 1981 opinion in an appeal of an administrative law judge's decision in *In re William R. Carter & Charles J. Johnson, Jr.*[10] In *Carter & Johnson*, two lawyers were integrally involved in drafting disclosure documents and public statements on behalf of a public company, which were ultimately shown to be false and misleading. The Commission, however, dismissed disciplinary proceedings against the two lawyers, explaining:

> If a securities lawyer is to bring his best independent judgment to bear on a disclosure problem, he must have the freedom to make innocent—or even, in certain cases, careless—mistakes without fear of legal liability or loss of the ability to practice before the Commission. Concern about his own liability may alter the balance of his judgment in one direction as surely as an unseemly obeisance to the wishes of his client can do so in the other. . . . Lawyers who are seen by their clients as being motivated by fears for their personal liability will not be consulted on difficult issues.[11]

The Commission reaffirmed this approach in 2008, when it applied the reasoning in *Carter & Johnson* to a litigated administrative enforcement action involving a lawyer. In *In re Scott G. Monson*, the Commission upheld the decision of an administrative law judge to dismiss cease-and-desist proceedings against an in-house lawyer at a broker-dealer who provided advice relating to the timing of certain mutual fund trades facilitated by the broker-dealer which was allegedly in violation of the Investment Company Act of 1940.[12]

3. Gutfreund 21(a) Report, Urban Decision, and Recent Trading and Markets Division Guidance: Lawyers as Supervisors

Commission precedent establishes that lawyers are not allowed to ignore violations of the federal securities laws without any repercussions. For example, in 1992, in the fallout from the submission by Salomon Brothers of numerous false bids in a series of Treasury Department auctions, the Commission addressed the behavior of the firm's general counsel who had become aware of the conduct. In *In re John H. Gutfreund et al.*,[13] the Commission addressed counsel's role in the matter by way of a report pursuant to Section 21(a) of the Securities Exchange Act of 1934 (''Exchange Act''), issued simultaneously with an administrative enforcement action against three other non-lawyer senior officers of the company. The report spoke to a lawyer's responsibility to respond appropriately to misconduct. The Commission made clear that once the lawyer learns of such misconduct, even if he or she is not a supervisor within the traditional sense of that term under Section 15 of the Exchange Act, the lawyer must take appropriate affirmative steps to address the situation, such as directing or monitoring an investigation of the conduct, making recommendations to limit the activities of those involved, or instituting procedures designed to prevent and deter future misconduct, and ensuring that such recommendations or procedures have been implemented.[14]

Ironically, in one recent example of a lawyer taking reasonable action in response to learning about a subordinate-broker's misconduct, the SEC still pursued enforcement action against the lawyer. *In re Theodore W. Urban*[15] involved a general counsel of a registered broker-dealer and investment advisor who recommended termination of a broker after learning of ''red flags,'' and had his compliance staff file a report with the New York Stock Exchange regarding unauthorized trading.[16] Nevertheless, the staff of the Commission recommended, and the Commission authorized, charges against the lawyer. An administrative law judge, however, dismissed cease-and-desist proceedings against the general counsel, finding that he had acted reasonably in connection with his supervisory responsibilities.[17] Notwithstanding the strength of the initial decision issued by the agency's Chief Administrative Law Judge Brenda Murray, the staff appealed. Ultimately, an evenly divided Commission affirmed the dismissal without an opinion,[18] a result which means that the initial decision ''shall be of no effect.''[19]

This case, perhaps as much as any action pursued by the staff in recent years, demonstrates the perils to the bar of an aggressive program directed at challenging lawyers' advice or conduct. The time, cost, and professional and personal damage inflicted on a lawyer who may eventually be vindicated by appealing an enforcement action cannot be overstated.

In likely response to the uncertain scope of supervisory liability for lawyers under Section 15 of the Exchange Act after *Urban*, the staff of the Division of Trading and Markets recently issued public guidance for practitioners.[20] The staff explained that the Commission has brought failure to supervise actions against legal or compliance personnel only where those individuals have assumed or been delegated supervisory responsibility over particular activities or situations and that ''[a]s a general matter, the staff does not single out compliance or legal personnel.''[21] The staff also made clear that legal and compliance personnel do not automatically attain supervisory responsibility under the Exchange Act for executing their duties in the ordinary

[10] 22 S.E.C. Docket 292, Rel. No. 17597, 1981 WL 384414 (Feb. 28, 1981).

[11] *Id.* at *25.

[12] 93 S.E.C. Docket 1898, Rel. No. 28323, 2008 WL 2574441 (June 30, 2008) (citing to *Carter & Johnson*, ''Given these considerations, we eschewed a standard that would expose an attorney to professional discipline 'merely because his advice, followed by the client, is ultimately determined to be wrong.' The intent requirement, we said, is crucial to an allegation of wrongdoing by a lawyer because it 'provides the basis for distinguishing between those professionals who may be appropriately considered as subjects of professional discipline and those who, acting in good faith, have merely made errors of judgment or have been careless.' '')

[13] 51 S.E.C. Docket 93, Rel. No. 31554, 1992 WL 362753 (Dec. 3, 1992).

[14] *Id.* at *16.

[15] 99 S.E.C. Docket 994, Rel. No. 402, 2010 WL 3500928 (ALJ Sept. 8, 2010) (initial order).

[16] *Id.* at 54.

[17] *Id.* at 53-57.

[18] *In re Theodore W. Urban*, 102 S.E.C. Docket 3284, Rel. No. 66259, 2012 WL 1024025 (Jan. 26, 2012).

[19] 17 C.F.R. § 201.411(f).

[20] SEC Division of Trading and Markets, *Frequently Asked Questions about Liability of Compliance and Legal Personnel at Broker-Dealers under Sections 15(b)(4) and 15(b)(6) of the Exchange Act* (Sept. 30, 2013), http://www.sec.gov/divisions/marketreg/faq-cco-supervision-093013.htm#11.

[21] *Id.*

course, such as providing legal advice to line business personnel, establishing and implementing a compliance program, sitting on a management committee, or providing advice to senior management.[22] It remains to be seen what impact, if any, this guidance will have on the Enforcement Division as it pursues investigations.

4. Sarbanes-Oxley: Refocus on Gatekeepers, including Lawyers

As a new wave of corporate scandals came to light in the early 2000s, the Enforcement Division turned again to scrutinizing lawyer conduct, this time with the help of Congress. Passed in 2002, the Sarbanes-Oxley Act raised the bar for lawyer conduct with its focus on ''gatekeepers,'' i.e., the professionals such as auditors or lawyers who help to ensure the markets are operating fairly. The statute requires lawyers to ''report up'' misconduct if they have evidence of material violations of the federal securities laws.[23] The SEC has since aggressively pursued enforcement actions against lawyers not only for their participation in allegedly wrongful conduct, but also for conduct that is, generally speaking, a typical function of a securities lawyer, such as preparing public disclosures or reporting to a company's board of directors.[24]

5. The SEC's Enforcement Manual: Memorializing Approach to Privilege

First published in the fall of 2008, the SEC's internal Enforcement Manual provides guidance on a variety of issues involving Enforcement Division operations. Many of the matters addressed by the Manual simply memorialized past practices; however, several provisions relating to how the staff should approach assertions of the attorney-client privilege were noteworthy. In particular, although the published guidance encourages the staff to ''respect'' assertions of privilege,[25] the Enforcement Manual and, broadly speaking, Commission policy, rewards entities and individuals under investigation for voluntarily disclosing privileged information[26] and ''all relevant underlying facts within [a party's] knowledge.''[27] So when a client hears the staff say emphatically that ''we're not asking for a privilege waiver, but we need all relevant factual information,'' the client will likely have to consider carefully whether to waive in order to get credit for cooperation.[28]

In addition, the published guidance has encouraged the staff to be more demanding and more aggressive in challenging privilege assertions in an investigation. For example, in a change to past practice, we have seen the staff request privilege logs on a rolling basis early in investigations before many of the facts have been developed and shortly after document productions have begun. Once those logs are submitted, the staff has become increasingly aggressive in testing privilege calls and arguing against the privilege assertions.[29]

6. Post-Madoff Developments and Enforcement Director Khuzami's Speech to Criminal Defense Lawyers

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[22] *See, e.g.*, *id.* (''Compliance and legal personnel do not become 'supervisors' solely because they have provided advice or counsel concerning compliance or legal issues to business line personnel, or assisted in the remediation of an issue.'')

[23] 15 U.S.C. § 7245. The Commission's prior guidance on this topic, as expressed in the *Gutfreund* 21(a) report, was that lawyers may consider – but are not required – taking additional steps in accordance with their professional and ethical obligations as lawyers: ''If such a person takes appropriate steps but management fails to act and that person knows or has reason to know of that failure, he or she should consider what additional steps are appropriate to address the matter. These steps may include disclosure of the matter to the entity's board of directors, resignation from the firm, or disclosure to regulatory authorities.'' *In re Gutfreund*, at *16 & n.26.

[24] *See, e.g.*, Stephen Cutler, SEC Enforcement Dir., The Themes of Sarbanes-Oxley as Reflected in the Commission's Enforcement Program (Sept. 20, 2004), http://www.sec.gov/news/speech/spch092004smc.htm (noting that the SEC had named lawyers as respondents or defendants in over 30 enforcement actions over the past two years); Phyllis Diamond, *Lawyers as Enforcement Targets Sparks Debate at Legal Gathering*, BNA Sec. Reg. & L. Rep. (Dec. 6, 2004). For an example of an enforcement action related to a lawyer's gatekeeping function, see *In re John E. Isselmann, Jr.*, Rel. No. 2108, 83 S.E.C. Docket 2413, 2004 WL 2114057 (Sept. 23, 2004) (former general counsel of a publicly traded technology manufacturer settled charges that he had allegedly failed to provide information about an accounting transaction to the company's Board of Directors, Audit Committee, and its outside auditors, as well as failing to communicate legal advice about the transaction to auditors).

[25] *See* SEC Office of Chief Counsel, SEC Enforcement Manual § 4.3 (Nov. 1, 2012), http://www.sec.gov/divisions/enforce/enforcementmanual.pdf (''The Staff must respect legitimate assertions of the attorney-client privilege and attorney work product protection. As a matter of public policy, the SEC wants to encourage individuals, corporate officers and employees to consult counsel about potential violations of the securities laws. Likewise, non-factual or core attorney work product – for example, an attorney's mental impressions or legal theories – lies at the core of the attorney work product doctrine.'')

[26] *See id.* (''Both entities and individuals may provide significant cooperation by *voluntarily* disclosing information. Voluntary disclosure need not include a waiver of privilege to be an effective form of cooperation and a party's decision to assert a legitimate claim of privilege will not negatively affect their claim to credit for cooperation. However, as discussed below, if a party seeks cooperation credit for timely disclosure of relevant facts, the party must disclose all such facts within the party's knowledge.''); *id.* (''To earn such credit, however, the corporation does need to produce, and the staff always may request, relevant factual information–including relevant factual information acquired through [privileged] interviews'').

[27] *See id.* (''A party's decision to assert a legitimate claim of attorney-client privilege or work product protection will not negatively affect their claim to credit for cooperation. The appropriate inquiry in this regard is whether, notwithstanding a legitimate claim of attorney-client privilege or work product protection, the party has disclosed all relevant underlying facts within its knowledge.'')

[28] Under changes made in August 2008 to Justice Department's Principles of Federal Prosecution of Business Organizations, cooperation in a federal criminal investigation does not depend on whether a company has waived attorney-client privilege or work product. U.S. Attorneys' Manual § 9-28.710-20. Indeed, federal prosecutors may not request non-factual or core attorney work product as a condition for cooperation credit. *Id.* at § 9-28.720. Under prior guidance, whether the corporation had waived attorney-client privilege or work product protections was a factor in criminal charging decisions. *See* Memorandum from Larry D. Thompson, Deputy Att'y General, on Principles of Federal Prosecution of Business Organizations to Heads of Department Components and United States Attorneys (Jan. 20, 2003).

[29] *See* SEC Enforcement Manual, *supra* note 25, at § 3.2.6.2.4 (''With respect to each document that has been withheld from production on the grounds of any privilege or protection, the staff should request that a detailed privilege log be produced at the same time as the responsive documents. A failure to provide sufficient information to support a claim of privilege can result in a waiver of the privilege.'').

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In the aftermath of the financial crisis during 2007 and 2008, and the discovery of the Bernard Madoff fraud in late 2008, there was enormous criticism and public and Congressional pressure on the SEC to round up the culprits and punish them harshly. In February 2009, the Commission appointed Robert Khuzami, then-general counsel for the Americas at Deutsche Bank AG and a former federal prosecutor, to lead the Enforcement Division. The choice of Khuzami was seen by many as both a reaction to the Commission's prior delay in discovering the Madoff fraud and the public's desire to see the SEC act more like a criminal law enforcement agency in cracking down on fraudulent conduct.[30] Khuzami moved quickly to overhaul the Enforcement Division. He attempted to streamline operations, pushing more decision making to the front lines and he hired more federal prosecutors in key positions. In addition, the Commission also delegated to the Enforcement Director the authority to issue formal orders of investigation, the agency action that authorizes the staff to issue subpoenas, and the authority to enforce those subpoenas in federal court. Both such actions had previously been the exclusive prerogative of the Commissioners, requiring the Presidential appointees to authorize such actions.

In 2011, Khuzami gave a speech to a group of white collar criminal defense lawyers where he roundly criticized defense counsel behavior during SEC investigations.[31] He focused on several areas where he said the Staff had seen an uptick in questionable practices: (1) multiple representations of witnesses in the same investigation who appeared to have adverse interests or who repeated the same implausible explanation of events; (2) witnesses who appeared to have no recollection of relevant events or recalled only exculpatory facts; (3) counsel who signaled to clients during testimony; and (4) counsel gaming the document production process by withholding documents on the basis of a privilege review, only to later produce those documents after key witnesses had already testified. In response, Khuzami said he would increase the number of referrals to the SEC's Office of General Counsel for obstructionist conduct. He closed by noting: ''The staff shares with each other their experiences with certain lawyers or firms. Senior managers also listen closely to staff who bear the brunt of the tactics I've described. Lawyers contemplating sharp practices should ask themselves what kind of reputation, and what level of credibility, they want to have with the staff, and whether that matters to them—and to their clients.''[32]

While there has been no empirical data reflecting the impact this speech has had on either the staff or the defense bar, there have been a number of anecdotal stories that have circulated throughout the defense bar about what seemed to be extraordinarily aggressive behavior of the staff in reaction to Khuzami's comments. The defense bar has generally viewed this speech as painting with too broad a brush.

7. Actions Where Lawyers Have Allegedly Participated in a Fraud

As noted, lawyers are not—and should not be—immune from enforcement actions just because they are lawyers. Any active participant in a fraud should face the consequences. In one recent case, for example, a lawyer for a prospective witness in an administrative proceeding was permanently barred from practicing before the SEC for offering to have his client evade service of a SEC subpoena and testify falsely in exchange for a financial package from other respondents in the proceeding.[33] The SEC has also pursued an action against an in-house lawyer for coaching employees to conceal in interviews with the government and outside counsel, the existence of accounting fraud.[34] Enforcement actions against lawyers who allegedly either traded while in possession of material non-public information or tipped others are legion,[35] and the SEC has actively pursued actions involving lawyers related to backdating stock option grants,[36] or allegedly participating in the issuance of false or misleading public statements.[37]

[30] *See, e.g.*, Phyllis Diamond, *Former Prosecutor Khuzami Named SEC Enforcement Director*, BNA Sec. Reg. & L. Rep. (Feb. 23, 2009) (citing statement by SEC Commissioner Mary Schapiro that ''[a]s a former federal prosecutor, Rob is well-suited to lead the SEC's Division of Enforcement as we continue to crack down on those who would betray the trust of investors.'')

[31] Robert Khuzami, SEC Enforcement Dir., Remarks to Criminal Law Group of the UJA-Federation of New York (June 1, 2011), http://www.sec.gov/news/speech/2011/spch060111rk.htm.

[32] *Id.* On this point it is worth noting the following recent remarks by Co-Director of Enforcement Andrew Ceresney about defense counsel: ''Any defense lawyer appearing before agency enforcement officials must provide all relevant information in the case, provide a thorough analysis of the facts and be wholly honest with the SEC staff. SEC personnel speak among themselves about those defense lawyers who are trustworthy and those who are not.'' Stephen Joyce, *Ceresney Provides Advice to Defense Counsel About SEC Changes in Enforcement Function*, BNA Sec. Reg. & L. Rep. (Oct. 1, 2013).

[33] *In re Steven Altman*, 99 S.E.C. Docket 2744, Rel. No. 63306, 2010 WL 5092725 (Nov. 10, 2010).

[34] Press Release, SEC, *SEC v. Computer Associates Int'l, Inc.*, Litig. Rel. No. 18891, 2004 WL 2109232 (Sept. 22, 2004). More recently, a former outside counsel who obstructed an SEC investigation by providing false testimony and altering documents was sentenced to 7 years in prison. *Attorney Who Obstructed SEC Probe Sentenced to Seven-Year Prison Term*, 8 White Collar Crime Report 690, Oct. 4, 2013.

[35] *See, e.g.*, Press Release, SEC, *Attorney, Wall Street Trader, and Middleman Settle SEC Charges in $32 Million Insider Trading Case*, Litig. Rel. No. 22345 (Apr. 25, 2012) (former outside counsel settled SEC charges related to insider trading in advance of at least 11 merger and acquisition announcements involving clients of law firm where he worked); Press Release, SEC, *Former Ernst & Young Partner and Former Stockbroker Settle SEC Insider Trading Charges*, Litig. Rel. No. 21629 (Aug. 18, 2010) (former partner and attorney at Big 4 accounting firm settled charges related to tipping a stockbroker friend with the identities of 7 acquisition targets of the firm's valuation services clients); Press Release, SEC, *Attorneys Arthur J. Cutillo and Jason C. Goldfarb Settle SEC Insider Trading Charges*, Litig. Rel. No. 22135 (Oct. 20, 2011) (former law firm attorney settled charges related to tipping an attorney-friend with information about at least 4 corporate acquisitions involving law firm's clients); Press Release, SEC, *SEC v. Tibor Klein et al.*, Litig. Rel. No. 22803 (Sept. 20, 2013) (alleging that after he ''became intoxicated,'' outside counsel disclosed information about the merger of one his law firm's clients to his financial advisor).

[36] *See, e.g.*, Press Release, SEC, *SEC Settles Options Backdating Charges With Former Apple General Counsel for $2.2 Million*, Litig. Rel. No. 20683 (Aug. 14, 2008) (former general counsel of major global technology company settled charges related to multiple instances of backdating of stock option grants to company executives); Press Release, SEC, *SEC v.*

Drawing the line at the right place in challenging improper and illegal behavior, whether involving the lawyer's defense in an investigation or the everyday counseling of a client, is often neither simple nor clear cut. When, for instance, things go wrong with a public company and the business suffers a reversal, accompanied by both mistakes and outright misconduct by some in the enterprise, any presumptive assault on the attorney's advice and role should only be based on compelling concerns, supported by evidence indicating that the lawyer was involved in the violative behavior.

Consequences - What This Means for Practitioners and Their Clients

The incentives of the SEC's cooperation policy and statements by senior SEC officials can have the unintended effect of encouraging a level of aggressiveness by the staff that may or may not be appropriate to a particular situation. That aggressiveness may chill the appropriate zealousness with which defense counsel should properly be approaching their role. The fear of being second-guessed by Enforcement staff for reasonable decisions made in good faith increases the pressure both on clients and their lawyers, not only on counseling matters in the ordinary course, but throughout any subsequent investigation. That concern may well unduly color the lawyer's advice about everything from strategy, representation of witnesses, or disclosures about the pending inquiry, to assertions of privilege and work product. These are serious risks to the role a lawyer is expected to play in representing a client's interests, as the subtle effects of being concerned about whether the staff may turn its focus on the lawyer cannot be ignored.

The reality is, however, that it is not uncommon in an SEC investigation for the staff to ask themselves whether the actions taken by lawyers or the advice given to clients were the product of good faith or some nefarious intent. Given that reality, practitioners must carefully consider, as part of their professional duties, how to navigate this environment with their clients. Indeed, notwithstanding any statements to the contrary by Commission officials about the staff not second-guessing the good faith professional judgments made by an attorney, the tendency by the staff to question any particular decision—with 20/20 hindsight—once there is a real problem with the events under review, is a serious concern.

Disclosure Issues. In certain matters focused on the question of disclosure, it will be particularly important to not only ensure that the correct decisions on the substance of the disclosure are made, but also that the context for the decisions are documented and available if a challenge is raised and waiver is on the table. Evidencing the process that was followed or the factual context to explain decisions made during a crisis, significant business event, or discovery of potential federal securities violations will help to address the concerns of a skeptical staff that is looking at the decisions only in hindsight. Practitioners and clients should consider:

- How is the decision making process being preserved? Does it capture the rationale, good faith, and/or reasonable thinking behind the decision making?
- What role are internal and external lawyers playing in the process? Could information that may be crucial to future defenses be viewed by regulators as being intentionally ''cloaked'' by privilege?
- How are public relations professionals and accounting experts (third-parties helping in the defense) being retained? Are there *Kovel*[38] letters? What about other non-lawyers? Are the roles and responsibilities of non-lawyers clear?
- What about the company's external auditors? Do they need to be made aware of any issues? How will communications be preserved by the client and its auditors? Will the auditors be provided with factual information, or information covered by the attorney-client privilege or work product doctrine?[39]

Discovery. During an SEC investigation, outside counsel needs to be cognizant of potential discovery landmines.

- Productions made pursuant to a limited privilege waiver will be scrutinized closely by other regulators and potential civil litigants.
- The SEC will not guarantee that others, including other federal agencies or civil litigants, will not try to gain access to otherwise privileged documents or infor-

Myron F. Olesnyckyj et al., Litig. Rel. No. 20056 (Mar. 27, 2007) (former general counsel of global online career and recruitment company settled charges related to backdating of stock option grants to thousands of company officers, directors, and employees).

[37] *See, e.g.*, *In re David C. Watt*, Rel. No. 46899, 2002 WL 31643064 (Nov. 25, 2002) (former general counsel of pharmaceutical company settled charges related to his participation in the drafting of misleading press release); Press Release, *SEC Settles Civil Injunctive Action Against Biopure Corporation and Its General Counsel*, Litig. Rel. No. 19825 (Sept. 12, 2006) (former general counsel of pharmaceutical company settled charges related to misleading public statements made about efforts to obtain FDA approval of company's products). Disclosure issues sometimes also arise in the insider trading context. In 2003, Martha Stewart was indicted on charges of conspiracy, obstruction of justice, and securities fraud, all linked to a personal stock trade she made in 2001. The securities fraud charges, which were later dismissed by the federal judge overseeing her trial, were based on Stewart's false and misleading public statements after the trade had become public, some of which had been issued by her attorneys in consultation with a public relations firm. *See Stewart Convicted on All Charges*, CNN.COM, Mar. 10, 2004, http://money.cnn.com/2004/03/05/news/companies/martha_verdict/; Press Release, Dep't of Justice *Martha Stewart and Her Broker Indicted by U.S. Grand Jury; Stewart Charged Separately with Securities Fraud* (June 4, 2003); *In re Grand Jury Subpoenas Dated March 24, 2003*, 265 F. Supp. 2d 321 (S.D.N.Y. 2003).

[38] Communications with public relations or other non-lawyer professionals may be protected by the attorney-client privilege if the non-lawyer's services are ''necessary, or at least highly useful'' for the effective consultation between the lawyer and the client. *United States v. Kovel*, 296 F.2d 918, 922 (2d Cir. 1961).

[39] Courts have held that although voluntary disclosure of information protected by the attorney-client privilege and/or the work product doctrine to an independent auditor waives attorney-client privilege, work-product protection is not necessarily waived. *See United States v. Deloitte LLP*, 610 F.3d 129, 139-140 (D.C. Cir. 2010).

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mation provided during an investigation. In fact, most courts hold that civil litigants can access documents that are disclosed to a governmental agency through a privilege waiver, even if the waiver was only intended for the initial investigation.[40]

■ Practitioners must ensure that productions made pursuant to a privilege waiver are accurate and complete, but also need to think carefully about and manage the risks of opening clients up to the possibility of additional claims.

Lawyers as Witnesses. In certain circumstances, lawyers need to be aware that they are in the danger zone—certainly as witnesses, if not as targets.

■ Outside counsel should prepare their clients (including in-house counsel) for the possibility that their communications may well become relevant in subsequent proceedings. (This goes for outside counsel, too.)

■ If lawyer communications are sought, then lawyers may well be witnesses in subsequent proceedings.

Privilege Issues. Address privilege issues early on in the production process, to avoid staff frustration with the process.

■ The staff is asking for privilege logs earlier in the production process, often far before practitioners have a good understanding of the all the facts and potential privilege issues.

■ Practitioners should ensure that senior lawyers are involved in assessing privilege calls at the outset of the investigation. This helps avoid changing privilege calls late in the production process or making the staff feel that inculpatory or ''interesting'' documents are deliberately being withheld.

■ It also helps practitioners to have the flexibility to make informed decisions about waiver during the production process and investigation.

Conclusion

We are in a new cycle of aggressive securities law enforcement and that may entail aggressive examination of lawyer conduct. While the staff in the past may have been reluctant to question a lawyer's advice or tactics so long as there was some apparent good faith premise underlying it, an increasingly skeptical staff pressured by an increasingly demanding Commission, Congress, and public is now more pointedly pressing for privilege waivers and examining and critiquing professional behavior. This means that if the staff believes they need non-privileged facts found in documents that lawyers have reviewed, edited, or approved or if the staff thinks it needs to interview lawyers who may possess relevant facts, they will pursue those avenues of investigation. Practitioners and clients need to be sensitive to these issues prior to and during investigations and think through a strategy that anticipates the level of second-guessing that may ensue in an investigation. If clients and counsel are able to navigate the actual and potential landmines inherent in the investigative process, this will increase the likelihood that they will be able to engage on and meaningfully address the merits of the staff's concerns, while avoiding many of the serious risks highlighted above.

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[40] *See, e.g.*, *In re Qwest Commc'ns Int'l Inc. Sec. Litig.*, 450 F.3d 1179, 1193 (10th Cir. 2006) (rejecting application of limited waiver where company produced over 220,000 pages of documents protected by the attorney-client privilege and work product doctrine to the DOJ and SEC during investigation while civil securities actions were outstanding). Federal Rule of Evidence 502 offers some protection if otherwise privileged documents are produced to the SEC or DOJ, but those documents are still discoverable by third parties. And unless the investigation has reached the litigation stage, further protections are unavailable. *See, e.g.*, FED. R. EVID. 502(d) (''A federal court may order that the privilege or protection is not waived by disclosure connected with the litigation pending before the court – in which event the disclosure is also not a waiver in any other federal or state proceeding.'')