



"Sarbanes-Oxley Made Me a Snitch" (And Other Myths from a Post-Enron World)

Like a juicy urban legend, misconceptions over Sarbanes-Oxley continue to swirl across the legal landscape. Misconception mania reached a fevered pitch this past fall and winter as final rules were promulgated — and the ABA weighed in with some hotly debated Model Rule changes.

Like something from an episode of *The Sopranos*, many in the legal community began fearfully imagining the day they'd have to "rat out" a long-time corporate client. But, in the end, has Sarbanes-Oxley rewritten the rules for attorney confidentiality and loyalty? Let's take a look.

What We Know

As of press time, the final SEC rules on lawyer conduct contain a "reporting up" requirement, specifically requiring an attorney to report evidence of a material violation of securities law or breach of fiduciary duty by the company. That report must be made to the chief legal officer and the chief executive officer of the company.

If the counsel or officer does not respond appropriately to the evidence, the attorney is required to report the evidence to the audit committee of the board of directors or to another committee of the board of directors comprised solely of directors not employed directly or indirectly by the issuer, or to the board of directors. Note that the proposed "reporting out" requirement — which, in some circumstances, would have obligated the lawyer to not only go up the corporate ladder but also to resign and report the resignation to the SEC — has been shelved.

Now here's where the myths begin to swirl.

Myth: "I'll have to snitch on my clients."

First and foremost, the rules as currently promulgated do not require attorneys to snitch on anyone. The so-called "Noisy Withdrawal Proposal" (Sec. 307) *would* have required attorneys to provide withdrawal notification to the SEC in most instances, providing reasons for the withdrawal. In fact, that proposal has been shelved. Conventional wisdom holds that the Justice Department and SEC are in a "wait-and-see" mode, watching to see if the current rules are sufficient.

Myth: "I can simply let someone on the board know about the problems."

Now this *is* a myth. While Sarbanes-Oxley does provide attorneys the ability to report to the board, it does not mean you can simply chat up a friendly board member or even a small faction of them. Once you report the breach to the CEO or CLO and determine his or her response is insufficient, you must present to the Audit Committee, the full board or to a QLCC (Qualified Legal Compliance Committee).

Myth: "Once I 'report up the ladder,' my duty is done."

Now here is a clear instance in which Sarbanes-Oxley *will* require a significant departure from what many attorneys are used to. Certainly, in the past, attorneys would inform someone of suspected problems as a simple matter of common sense (and self-preservation). But Sarbanes-Oxley now requires lawyers to not only make the report, but also to basically remain as a watchdog and evaluate the sufficiency of the corporation's response to the breach.

If the response is deemed insufficient, the attorney must take further action. Lawyers are excused from performing this "watchdog" function in only two circumstances. The first is where the lawyer is a "supervised attorney," in which case the evidence may simply be reported to his or her "supervisory attorney." The lawyer may also report the evidence directly to a QLCC.

Myth: "But won't that make me a 'mole' for the SEC?"

We need to be very clear here: The lawyer does not suddenly switch allegiances and become a spy for the SEC — which would be a clear-cut violation of the lawyer's duty to the client. The attorney's duty of loyalty and confidentiality

remains with the client and *not* to outsiders, including regulators and shareholders. Only in the instance where a lawyer has evidence that the client is using the lawyers' services to carry out criminal or fraudulent activities is the lawyer permitted to blow the whistle to "outsiders."

Myth: "Sarbanes-Oxley has radically changed the way most attorneys practice."

Hardly. Adopted in its final form, the Act didn't change lawyers' responsibilities in the roughly 30 to 40 states that had similar rules on the books. Most states already had some mechanism that allowed lawyers to "report" clients suspected of violating securities laws (albeit, not in a very loud or direct way) by at least disavowing work done on behalf of that client.

Myth: "Sarbanes-Oxley violates attorney-client confidentiality."

Because the Act does *not* require an attorney to report evidence of the violations to the SEC, or to any agency or entity other than those within the corporation itself, reporting within a corporate structure presumably would not be a violation of the attorney-client privilege.