

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 205

[Release Nos. 33-8185; 34-47276; IC-25919; File No. S7-45-02]

RIN 3235-A172

Implementation of Standards of Professional Conduct for Attorneys

AGENCY: Securities and Exchange Commission.

ACTION: Final rule.

SUMMARY: The Securities and Exchange Commission ("Commission") is adopting a final rule establishing standards of professional conduct for attorneys who appear and practice before the Commission on behalf of issuers. Section 307 of the Sarbanes-Oxley Act of 2002 requires the Commission to prescribe minimum standards of professional conduct for attorneys appearing and practicing before the Commission in any way in the representation of issuers. The standards must include a rule requiring an attorney to report evidence of a material violation of securities laws or breach of fiduciary duty or similar violation by the issuer up-the-ladder within the company to the chief legal counsel or the chief executive officer of the company (or the equivalent thereof); and, if they do not respond appropriately to the evidence, requiring the attorney to report the evidence to the audit committee, another committee of independent directors, or the full board of directors. Proposed Part 205 responds to this directive and is intended to protect investors and increase their confidence in public companies by ensuring that attorneys who work for those companies respond appropriately to evidence of material misconduct. We are still considering the "noisy withdrawal" provisions of our original proposal under section 307; in a related proposing release we discuss this part of the original proposal and seek comment on additional alternatives.

EFFECTIVE DATE: August 5, 2003.

FOR FURTHER INFORMATION CONTACT: Timothy N. McGarey or Edward C. Schweitzer at 202-942-0835.

I. Executive Summary

Section 307 of the Sarbanes-Oxley Act of 2002 (the "Act") (15 U.S.C. 7245)¹

mandates that the Commission issue rules prescribing minimum standards of professional conduct for attorneys appearing and practicing before it in any way in the representation of issuers, including at a minimum a rule requiring an attorney to report evidence of a material violation of securities laws or breach of fiduciary duty or similar violation by the issuer or any agent thereof to appropriate officers within the issuer and, thereafter, to the highest authority within the issuer, if the initial report does not result in an appropriate response. The Act directs the Commission to issue these rules within 180 days.²

On November 21, 2002, in response to this directive, we published for comment proposed Part 205, entitled "Standards of Professional Conduct for Attorneys Appearing and Practicing before the Commission in the Representation of an Issuer." The proposed rule prescribed minimum standards of professional conduct for attorneys appearing and practicing before us in any way in the representation of an issuer. The proposed rule took a broad view of who could be found to be appearing and practicing before us. It covered lawyers licensed in foreign jurisdictions, whether or not they were also admitted in the United States. In addition to a rigorous up-the-ladder reporting requirement, the proposed rule incorporated several corollary provisions. Under certain circumstances, these provisions permitted or required attorneys to effect a so-called "noisy withdrawal" by notifying the Commission that they have withdrawn from the representation of the issuer, and permitted attorneys to report evidence of material violations to the Commission.

Our proposing release³ generated significant comment and extensive debate. We received a total of 167 timely

for attorneys appearing and practicing before the Commission in any way in the representation of issuers, including a rule—

(1) Requiring an 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 chief legal counsel or the chief executive officer of the company (or the equivalent thereof); and

(2) If the counsel or officer does not appropriately respond to the evidence (adopting, as necessary, appropriate remedial measures or sanctions with respect to the violation), requiring the attorney to report the evidence to the audit committee of the board of directors of the issuer 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.

² President Bush signed the Act on July 30, 2002.

³ See Release 33-8150 (Nov. 21, 2002), 67 FR 71669 (Dec. 2, 2002).

comment letters: 123 from domestic parties and 44 from foreign parties. In addition to soliciting comments, on December 17, 2002 the Commission hosted a Roundtable discussion concerning the impact of the rules upon foreign attorneys. Many of these comments focused on the following issues: The scope of the proposed rule (including, particularly, its application to attorneys who either are not admitted to practice in the United States, or are admitted in the United States but who do not practice in the field of securities law); the proposed rule's "noisy withdrawal" provision (including the Commission's authority to promulgate this portion of the rule and the provision's impact upon the attorney-client relationship); and the triggering standard for an attorney's duty to report evidence of wrongdoing. In light of the compressed time period resulting from the 180-day implementation deadline prescribed in the Act, a number of commenters requested that the Commission allow additional time for consideration of several aspects of the proposed rule, including the application of the rule to non-United States lawyers and the impact of the "noisy withdrawal" and related provisions.

The thoughtful and constructive suggestions we have received from a broad spectrum of commenters have enabled us better to understand interested parties' views concerning the operation and impact of the proposed rule. As more specifically discussed below, the final rule we adopt today has been significantly modified in light of these comments and suggestions. Thus, the triggering standard for reporting evidence of a material violation has been modified to clarify and confirm that an attorney's actions will be evaluated against an objective standard. The documentation requirements imposed upon attorneys and issuers under the proposed rule have been eliminated, and a "safe harbor" provision has been added to protect attorneys, law firms, issuers and officers and directors of issuers. In response to the large number of comments requesting that we defer the immediate implementation of a final rule to accord affected persons adequate time to assess the duties imposed thereunder, we have deferred the effective date of the rule until 180 days after publication in the **Federal Register**.

We believe that the final rule responds fully to the mandate of Section 307 to require reporting of evidence of material violations up-the-ladder within an issuer, thereby allowing issuers to take necessary remedial action expeditiously and reduce any adverse

¹ Section 307 of the Sarbanes-Oxley Act of 2002 (the "Act") (15 U.S.C. 7245) mandates that the Commission: Shall issue rights, in the public interest and for the protection of investors, setting forth minimum standards of professional conduct