

objectives the lawyer must pursue, even when unwise, so long as they are not illegal or unethical. However, we disagree with the comment to the extent it suggests counsel is never charged with acting in the best interests of the issuer. ABA Model Rule 1.13 provides that an attorney is obligated to act in the "best interests" of an issuer in circumstances contemplated by this rule: that is, when an individual associated with the organization is violating a legal duty, and the behavior "is likely to result in substantial injury" to the organization. In those situations, it is indeed appropriate for counsel to act in the best interests of the issuer by reporting up-the-ladder.⁶⁹ However, the Commission appreciates that, with respect to corporate decisions traditionally reserved for management, counsel is not obligated to act in the "best interests" of the issuer. Thus, the reference in the proposed rule to the attorney having a duty to act in the best interests of the issuer has been deleted from the final rule. The sentence has also been modified to make it clear the lawyer "owes his or her professional and ethical duties to the issuer as an organization."

As to the second concern, the courts have recognized that counsel to an issuer does not generally owe a legal obligation to the constituents of an issuer—including shareholders.⁷⁰ The Commission does not want the final rule to suggest it is creating a fiduciary duty to shareholders that does not currently exist. Accordingly, we have deleted from the final rule the reference to the attorney being obligated to act in the best interest of shareholders. This modification should also address the third concern as the Commission does not intend to create a private right of action against attorneys or any other

person under any provision of this part. Indeed, the final rule contains a new provision, 205.7, that expressly provides that nothing in this part is intended to or does create a private right of action.

205.3(b) provides:

(b) *Duty to report evidence of a material violation.* (1) If an attorney, appearing and practicing before the Commission in the representation of an issuer, becomes aware of evidence of a material violation by the issuer or by any officer, director, employee, or agent of the issuer, the attorney shall report such evidence to the issuer's chief legal officer (or the equivalent thereof) or to both the issuer's chief legal officer and its chief executive officer (or the equivalents thereof) forthwith. By communicating such information to the issuer's officers or directors, an attorney does not reveal client confidences or secrets or privileged or otherwise protected information related to the attorney's representation of an issuer.

Section 205.3(b) clarifies an attorney's duty to protect the interests of the issuer the attorney represents by reporting within the issuer evidence of a material violation by any officer, director, employee, or agent of the issuer. The section was broadly approved by commenters. Paragraph (b)(1) describes the first step that an attorney representing an issuer is required to take after he or she becomes aware of evidence of a material violation, now defined in § 205.2. The definition of "evidence of a material violation" originally proposed was controversial and has been modified (as discussed above). Paragraph (b)(1), however, was otherwise generally approved.⁷¹

Section 205.3(b)(2) in Proposed Rule: Withdrawn

(2) The attorney reporting evidence of a material violation shall take steps reasonable under the circumstances to document the report and the response thereto and shall retain such documentation for a reasonable time.

The language set forth from proposed subsection 205.3(b)(2) of the proposed rule has been withdrawn.

In the final rules we have eliminated all requirements that reports and responses be documented and maintained for a reasonable period. Under the proposed rule, a lawyer would have been required to document his or her report of evidence of a material violation (205.3(b)(2)); the CLO would have been required to document any inquiry in response to a report (205.3(b)(3)); a reporting attorney would

have been required to document when he or she received an appropriate response to a report (205.3(b)(2)); and an attorney who believed he or she did not receive an appropriate response to a report would have been required to document that response (205.3(b)(8)(ii)).

The Commission proposed the documentation requirements because it believed that up-the-ladder reporting would be handled more thoughtfully if those involved memorialized their decisions. It was also the Commission's view that documentation would benefit reporting attorneys as it would provide them with a contemporaneous written record of their actions that they could use in their defense if their up-the-ladder reporting subsequently became the subject of litigation. To that end, the Commission proposed 205.3(e)(1) (which is codified in the final rule as § 205.3(d)(1)) that specifically authorizes an attorney to use "[a]ny report under this section * * * or any response thereto * * * in connection with any investigation, proceeding, or litigation in which the attorney's compliance with this part is in issue." Moreover, the Commission noted (*see* note 52 to the proposing release) that in at least one reported judicial decision, an associate at a law firm who had memorialized his reasons for resigning from the firm over a dispute regarding the adequacy of disclosures in a registration statement, was dismissed as a defendant in subsequent litigation over the appropriateness of those disclosures because his contemporaneous record demonstrated he had not participated in the fraud.

Nevertheless, the comments that the Commission received to the proposed documentation requirements were almost unanimously in opposition to its inclusion in the final rule. A number of commenters expressed concern that the documentation requirement could be an impediment to open and candid discussions between attorneys and their issuer clients. Those commenters were of the view it would stultify the consultation process because if the client knows the lawyer is documenting discussions regarding a potential material violation, managers are less likely to be honest and forthcoming.⁷²

Other commenters expressed concern that the documentation requirement has the potential to create a conflict of interest between the lawyer and his or her client. For example, one commenter

⁶⁹ See ABA Model Rule 1.13, at 1:139.

⁷⁰ Decisions in a number of states recognize that, under state law, an attorney for an issuer does not owe a fiduciary duty to shareholders. *See Pelletier v. Zweifel*, 921 F.2d 1465, 1491–92 n.60 (11th Cir.) *cert. denied*, 502 U.S. 955 (1991) (Under Georgia law "[I]t is a black letter principle of corporation law that a corporation's counsel does not owe * * * [a] fiduciary duty to the corporation's shareholders"). *See also Skarbrevik v. Cohen, England & Whitfield*, 231 Cal. App. 3d 692, 703 (1991) (Under California law, "[a]n attorney representing a corporation does not become the representative of its stockholders merely because the attorney's actions on behalf of the corporation also benefit the stockholders; as attorney for the corporation, counsel's first duty is to the corporation."); *Egan v. McNamara*, 467 A.2d 733, 738 (DC 1983) ("According to the District of Columbia Code of Professional Responsibility (Code), an attorney represents, and therefore owes a duty to, the entity that retains him. * * * When retained to represent a corporation, he represents the entity, not its individual shareholders, officers, or directors.").

⁷¹ The Comment of Federal Bar Counsel, at 12–13, for example, objected to "becomes aware" in (b)(1) but appears to have done so in connection with the proposed definition of "evidence of a material violation." The revisions made to that definition appear to address those objections.

⁷² *See, e.g.*, Comments of the American Bar Association, at 22; Comments of the American Corporate Counsel Association, at 5; Comments of the Association of the Bar of the City of New York, at 16; Comments of Cleary, Gottlieb, Steen & Hamilton, at 6.