

where appropriate, modified the paragraph in a manner that responds to that concern. Subparagraph (iii) has been limited to material violations, and subparagraph (i) limits its application to material violations that are likely to cause substantial injury to the financial interest or property of the issuer or investors.

Finally, the Commission concludes that it is not appropriate for it to wait for further developments. The Commission believes there has been ample discussion of this paragraph in the comments received, and that the major issues concerning this paragraph have been well identified. In addition, delay pending further developments does not promise to be fruitful: most state supreme courts already have rules in place that are consistent with this paragraph, and there is no evidence when, if ever, state supreme courts (or legislative bodies) will revisit these issues, and the public interest in allowing lawyers appearing and practicing before the Commission to disclose the acts covered by this paragraph counsels against waiting indefinitely for further refinement of state ethics rules.

Subsection 205.3(e)(3) in Proposed Rule: Withdrawn

The proposed paragraph read:

Where an issuer, through its attorney, shares with the Commission information related to a material violation, pursuant to a confidentiality agreement, such sharing of information shall not constitute a waiver of any otherwise applicable privilege or protection as to other persons.

Several commenters stated that it was uncertain if the Sarbanes-Oxley Act granted the Commission the authority to promulgate a rule that would control determinations by state and federal courts whether a disclosure to the Commission, even if conditioned on a confidentiality agreement, waives the attorney-client privilege or work product protection,¹¹³ and a few suggested that the proposed paragraph would conflict with Federal Rule of Evidence 501.¹¹⁴ They noted that this is

an unsettled issue in the courts, or suggested that the Commission's proposed rule runs contrary to the bulk of decisional authority on this issue.¹¹⁵ A few also noted that proposed legislation before Congress in 1974, supported by the Commission, that would have enacted a provision permitting issuers to selectively waive privileges in disclosures to the Commission was ultimately not passed by Congress.¹¹⁶ The concern was expressed that attorneys might disclose information to the Commission in the belief that the evidentiary privileges for that information were preserved, only to have a court subsequently rule that the privilege was waived.¹¹⁷

The Commission has determined not to adopt the proposed rule on this "selective waiver" provision. The Commission is mindful of the concern that some courts might not adopt the Commission's analysis of this issue, and that this could lead to adverse consequences for the attorneys and

shall be governed by the principles of the common law as they may be interpreted by the courts of the United States in the light of reason and experience. However, in civil actions and proceedings, with respect to an element of a claim or defense as to which State law supplies the rule of decision, the privilege of a witness, person, government, State, or political subdivision thereof shall be determined in accordance with State law."

¹¹⁵ Comments of the American Bar Association, at 32 n. 21; Comments of Sheldon M. Jaffe, at 9–11; Comments of Edward C. Brewer, III, at 11; Comments of Latham & Watkins, at 5; Comments of Morrison & Foerster and eight other law firms, at 19.

¹¹⁶ Comments of the American Bar Association, at 32 n. 22; Comments of Morrison & Foerster and eight other law firms, at 19. The Commission notes that the proposal in Congress to which these commenters refer would have applied the selective waiver doctrine to all documents produced to the Commission, and was not limited to productions conditioned upon an express confidentiality agreement. See *Westinghouse Elec. Corp. v. Republic of the Philippines*, 951 F.2d 1414, 1425 (3d Cir. 1991). Also, Congress did not reject the Commission's proposal; rather, the House Committee to which the proposal was submitted took no action. See SEC Oversight and Technical Amendments: Hearing Before the Subcommittee on Telecommunications, Consumer Protection, and Finance of the House Committee on Energy and Commerce, 98th Cong., 2d Sess 341 at 34, 51 (1984). Therefore, that the proposal before that House Committee in 1984 was not ultimately enacted carries no significance. *NAACP v. American Family Mut. Ins. Co.*, 978 F.2d 287, 299 (7th Cir. 1992) ("unsuccessful proposals to amend a law, in the years following passage, carry no significance").

¹¹⁷ Comments of Richard W. Painter, at 9; Comments of Susan P. Koniak *et al.*, at 6; Comments of Latham & Watkins, at 5 ("[g]iven the high stakes associated with waiver of privilege, uncertainty as to interpretation of [Paragraph 205.3(e)(3)'s] requirements in this regard is troubling"); Comments of the SIA/TBMA at 15 ("[a]lthough we welcome this positive statement of Commission policy, given sharp disagreements among courts on the question of selective waiver, issuers and attorneys cannot be secure in their disclosures absent a statutory statement of express preemption").

issuers who disclose information to the Commission pursuant to a confidentiality agreement, believing that the evidentiary protections accorded that information remain preserved.

Nonetheless, the Commission finds that allowing issuers to produce internal reports to the Commission—including those prepared in response to reports under 205.3(b)—without waiving otherwise applicable privileges serves the public interest because it significantly enhances the Commission's ability to conduct expeditious investigations and obtain prompt relief, where appropriate, for defrauded investors. The Commission further finds that obtaining such otherwise protected reports advances the public interest, as the Commission only enters into confidentiality agreements when it has reason to believe that obtaining the reports will allow the Commission to save substantial time and resources in conducting investigations and/or provide more prompt monetary relief to investors. Although the Commission must verify that internal reports are accurate and complete and must conduct its own investigation, doing so is far less time consuming and less difficult than starting and conducting investigations without the internal reports. When the Commission can conduct expeditious and efficient investigations, it can then obtain appropriate remedies for investors more quickly. The public interest is thus clearly served when the Commission can promptly identify illegal conduct and provide compensation to victims of securities fraud.

The Commission also finds that preserving the privilege or protection for internal reports shared with the Commission does not harm private litigants or put them at any kind of strategic disadvantage. At worst, private litigants would be in exactly the same position that they would have been in if the Commission had not obtained the privileged or protected materials. Private litigants may even benefit from the Commission's ability to conduct more expeditious and thorough investigations. Indeed, many private securities actions follow the successful completion of a Commission investigation and enforcement action. Consequently, allowing the Commission access to otherwise privileged and inaccessible internal reports but denying access to others would not be unfair to private litigants but is appropriate in the public interest and for the protection of investors.

For these reasons, the Commission will continue to follow its policy of

¹¹³ Comments of Richard W. Painter, at 9 ("the only effective method" of assuring lawyers that the attorney-client privilege is not waived by disclosure to the Commission "is to seek an act of Congress establishing selective waiver and preempting inconsistent state law"); Comments of the American Bar Association, at 32; Comments of Susan P. Koniak *et al.*, at 44.

¹¹⁴ Comments of Sheldon Jaffe, at 10. Fed. R. Evid. 501 provides that "[e]xcept as otherwise required by the Constitution of the United States or provided by Act of Congress or in rules prescribed by the Supreme Court pursuant to statutory authority, the privilege of a witness, person, government, State, or political subdivision thereof