LEGAL ETHICS—SECURITIES—SECURITIES ATTORNEYS' AFFIRMATIVE DUTY TO TAKE PROMPT ACTION TO HAVE CLIENTS COMPLY WITH DISCLOSURE REQUIREMENTS. *In re Carter*, SEC Release No. 34-17597 (Feb. 28, 1981), [Current] FED. SEC. L. REP. (CCH) ¶ 82,847.

The Securities and Exchange Commission (Commission) in *In re Carter*[1] set forth ethical standards for securities lawyers who counsel corporate clients on disclosure requirements.[2] The Commission construed the "unethical or improper professional conduct" clause of rule 2(e) of its Rules of Practice[3] to require attorneys, faced with a "strong-willed" management that ignores their disclosure advice, to take prompt corrective action[4] within the client system—the corporate entity.[5] Prompt action can include, but is not limited to, bringing the matter before one or more members of the board of directors, the full board itself, or other officers or members of management, as well as resigning.[6] Failure to take affirmative action can lead to the inference that the attorney has been "co-opted" into a non-disclosure scheme.[7]

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[1] SEC Release No. 34-17597 (Feb. 28, 1981), [Current] FED. SEC. L. REP. (CCH) ¶ 82,847.

[2] *Id.* at 84,172. In dissent, Commissioner Evans thought that the Commission should not have promulgated the standard without first soliciting public opinion. *Id.* at 84,178 (Evans, Comm'r, concurring and dissenting). *See also* Miller, *The Distortion and Misuse of Rule 2(e)*, 7 SEC. REG. L.J. 54, 71 (1979).

[3] 17 C.F.R. § 201.2(e)(1) (1980) provides:

> The Commission may deny, temporarily or permanently, the privilege of appearing or practicing before it in any way to any person who is found by the Commission after notice of and opportunity for hearing in the matter (i) not to possess the requisite qualifications to represent others, or (ii) to be lacking in character or integrity or to have engaged in unethical or improper professional conduct, or (iii) to have willfully violated or aided and abetted the violation of any provision of the federal securities laws (15 U.S.C. 77a to 80b-20), or the rules and regulations thereunder.

Id.

"Practicing before the Commission" is broadly defined to include both the "transact[ion] [of] any business with the Commission" and "the preparation of any statement, opinion, or other paper" which forms part of any document filed with the Commission. *Id.* § 201.2(g).

[4] *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,172.

[5] *Id.* at 84,171.

[6] *Id.* at 84,172.

[7] *Id.*

The history of rule 2(e)[8] as an enforcement tool[9] reveals the evolution of the Commission's policy from self-regulation[10] by the securities bar to pervasive Commission regulation of the bar.[11] Initially the use of rule 2(e) was limited to practices involving intentional misconduct.[12] Since 1960 the Commission has expanded the scope of

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[8] Originally promulgated in 1935 as rule II, 1 Fed. Reg. 1,753 (1936), rule 2(e)(1) was adopted in June 1938 "in substantially similar form to its present-day prescriptions, with the exception that the subsection of the Rule covering disciplinary actions for willful violations of the federal securities laws was added in 1971." Miller, *supra* note 2, at 57.

[9] Among the Commission's "arsenal of enforcement tools" are "the explicit authority to seek injunctive relief against securities laws violations (Securities Act of 1933 § 20, and Securities Exchange Act of 1934 § 21); and the foremost enforcement power to refer evidence of securities laws to the Justice Department for criminal prosecution (Securities Act § 20(b) and Exchange Act § 21(e))." Miller, *supra* note 2, at 55 n.2.

[10] *See* Jennings, *Self-Regulation in the Securities Industry: The Role of the Securities and Exchange Commission*, 29 LAW & CONTEMP. PROB. 663 (1964). During the period of self-regulation from 1935 to 1960, primary reliance was placed upon the legal and accounting professions for the exercise of control and the proposal of reforms. Note, *SEC Disciplinary Hearings—* Touche Ross v. SEC—*Rule 2(e) Validated in First Public Proceeding: Uncertainty Ahead for Securities Practitioners*, 5 J. CORP. L. 433, 439 (1980).

> Attorneys have historically favored self-regulation and have considered rule 2(e) as more of a risk factor than the rules of the state or local bar. This is true not only because the SEC is essentially an enforcement body as opposed to a state bar disciplinary committee, which in most states is composed of an attorney's peers, who by nature have a common frame of reference with an offending attorney, but also because of the nature of the administrative agency structure which combines administrative, investigatory, prosecutorial, decisional, and rule-making functions in one body and "under one roof."

Johnson, *The Expanding Responsibilities of Attorneys in Practice Before the SEC: Disciplinary Proceedings Under Rule 2(e) of the Commission's Rules of Practice*, 25 MERCER L. REV. 637, 641-42 (1974). *See generally* Cheek, *Professional Responsibility and Self-Regulation of the Securities Lawyer*, 23 WASH. & L. L. REV. 598 (1975).

[11] *See generally* Miller, *supra* note 2, at 55. The evolution was accompanied by a dramatic increase in the number of disciplinary proceedings instituted by the Commission, from a total of only five cases prior to 1960 to over 85 cases since 1970. *In re* Keating, Muething & Klekamp, SEC Release No. 15,982 (July 8, 1979) [1979 Transfer Binder] FED. SEC. L. REP. CCH ¶ 82,124, at 81,994 (Karmel, Comm'r, dissenting).

The change in policy can be attributed to the Commission's

> [s]elf-professed inability to protect the financial community from the "monstrous financial debacles" which had occurred since 1960. The SEC was disturbed by the growing number of misleading and inaccurate documents accompanying public offerings that went undetected and led to investor injury. As a result of this post-1960 trend, the SEC began to exert pressure through 2(e) hearings upon practitioners to increase their vigilance in protecting the public interest.

Note, *supra* note 12, at 439-40. Underlying the Commission's movement away from its traditional philosophy was the realization that "with its small staff, limited resources, and onerous tasks [the Commission] is peculiarly dependent on the probity and the diligence of the professionals who practice before it." *In re* Emanuel Fields, SEC Release No. 5404 (June 18, 1973) [1973 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 79,407, at 83,175 n.20, *aff'd without opinion*, 495 F.2d 1085 (D.C. Cir. 1974). The Commission therefore concluded that it is "under a duty to hold our bar to appropriately rigorous standards of professional honor." *Id.*

[12] For an excellent discussion of the traditional view of the Commission regarding the responsibilities and duties of securities lawyers, see Lowenfels, *Expanding Public Responsibilities*

rule 2(e) beyond this limited application.[13] The Commission has held securities lawyers liable for negligence in the performance of their professional duties,[14] and has used consent sanctions[15] to have law firms voluntarily revise their internal operating procedures.[16] Representative of this trend is the Commission's action against the National Student Marketing Corp.,[17] where the Commission sought to impose a standard requiring "whistle-blowing," that is, notifying the Commission of a client's transgressions.[18] The district court ultimately did not

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of Securities Lawyers: An Analysis of the New Trend in Standard of Care and Priorities of Duties, 74 COLUM. L. REV. 412, 413-18 (1974). Lowenfels pointed out that both the courts and the Commission had a "traditional reluctance" against imposing sanctions or liabilities on securities lawyers unless they actively participated in blatant frauds. *Id.* at 414.

[13] *See* Johnson, *supra* note 10, at 644. As Johnson pointed out:

> As early as 1960, an intent by the Commission to expand the scope of Rule 2(e) became visible. . . . In *Morris Mac Schwebel* [40 SEC 347 (1960), *modified*, 40 SEC 459 (1961)] the defendant attorney failed, *inter alia*, to rectify deficient reports filed with the SEC and was permanently disqualified from practicing before the Commission. The Commission noted that "whether or not respondent intended to facilitate evasion of the law, his conduct evidenced at least a gross indifference to the observance of legal requirements which an attorney in particular would strive to foster. [*Id.* at 371].

Id.

[14] *See* SEC v. Universal Major Indus. Corp., [1973 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,212 (S.D.N.Y. 1973).

[15] A consent sanction is comprised:

> of an agreement between the individual practitioner or the practitioner's firm and the SEC setting forth guidelines and standards proposed by the SEC as a means for the professional or firm to upgrade disclosure procedures and avoid future misrepresentations. The consent sanction set[s] forth the desired levels of future conduct for the securities practitioner.

Note, *supra* note 10, at 440.

[16] *See In re* Keating, Muething & Klikamp, SEC Release No. 15982 (July 2, 1979) [1979 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 82,164. Regarding the Commission's policy toward accounting firms, Miller questions whether the true intent of the Commission is "to subjugate the accounting profession to the Commission's day-to-day control." Miller, *supra* note 2, at 68.

[17] The Commission's complaint was against National Student Marketing Corp. and numerous other defendants including four individual attorneys and two distinguished law firms. It resulted in numerous reported opinions, *e.g.*, SEC v. National Student Marketing Corp., 457 F. Supp. 682 (D.D.C. 1978); SEC v. National Student Marketing Corp., 430 F. Supp. 639 (D.D.C. 1977); SEC v. National Student Marketing Corp., 68 F.R.D. 157 (D.D.C. 1975), *aff'd*, 538 F.2d 404 (D.C. Cir. 1976), *cert. denied*, 429 U.S. 1073 (1977).

[18] The charges against Student Marketing Corp. derived:

> from the merger between NSMC [National Student Marketing Corporation] and Interstate National Corp., in which the Interstate shareholders exchanged their shares for approximately 1,650,000 shares of NSMC stock. Just before the merger closing, NSMC's accountants submitted a "comfort" letter to counsel for both parties that adjusted NSMC's nine months' earnings downward by $784,000 and converted a reported $700,000 profit into a net loss. Counsel for both parties declined to insist that the contents of this letter be publicized, declined to insist that Interstate's shareholders (whose approval of the merger had been solicited based on the erroneous profit report) be resolicited, and proceeded to consummate the merger. Imme-

endorse the whistle-blowing standard,[19] but instead held that securities attorneys have a duty to "speak out" to their clients regarding non-compliance with disclosure requirements.[20]

Although there has been some judicial support for the Commission's negligence standard,[21] such support came prior to the Supreme Court's decisions in *Ernst & Ernst v. Hochfelder*[22] and *Aaron v. SEC*,[23] which require scienter[24] in both damage actions[25] and suits for injunctive relief[26] under section 10(b) of the Securities and Exchange Act of 1934[27] and Rule 10b-5[28] promulgated thereunder. After *Hochfelder* and *Aaron*, a showing that a lawyer knowingly violated the securities laws may be required.[29]

Perhaps because of the lack of total endorsement of its objectives by the judiciary, the Commission took the opportunity in *In re Carter* to enunciate its standard for professional conduct—a standard less extreme than the previously proposed whistle-blowing duty.[30] The

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> diately following the closing, 77,000 shares of NSMC common stock were publicly sold by former Interstate directors for $1,900,000.

Lowenfels, *supra* note 11, at 420. For a thorough discussion of the major issues raised by the NSMC action see Patterson, *The Limits of the Lawyer's Discretion and the Law of Legal Ethics: National Student Marketing Revisited*, 1979 DUKE L.J. 1251.

[19] SEC v. National Student Marketing Corp., 457 F. Supp. 682, 714-15, 715 n.74 (D.D.C. 1978).

[20] *Id.* at 713.

[21] *See* SEC v. Spectrum Ltd., 489 F.2d 535 (2d Cir. 1973).

[22] 425 U.S. 185 (1976).

[23] 446 U.S. 680 (1980).

[24] Scienter was broadly defined in *Hochfelder* as "a mental state embracing intent to deceive, manipulate or defraud." 425 U.S. at 193 n.12. As regards the application of the scienter requirement to professionals in the securities field, some jurisdictions hold that reckless conduct satisfies the requirement and that the plaintiff can use circumstantial evidence to show that the professional-defendant did not have a genuine belief that the disclosed information was complete and accurate. *See* McLean v. Alexander, 599 F.2d 1190 (3d Cir. 1979).

[25] 425 U.S. at 193.

[26] 446 U.S. at 695. The court also held that scienter is a necessary element in injunctive actions under § 17(a)(1) of the Securities Act of 1933, 15 U.S.C. § 77q(a) (1977), but not under § 17(a)(2)(3). 446 U.S. at 697.

[27] Securities Exchange Act of 1934, 15 U.S.C. § 78(j) (1977).

[28] 17 C.F.R. § 240.10b-5 (1980).

[29] It should be noted that the standard of culpability in tender offer cases under § 14 of the Securities Exchange Act of 1934, 15 U.S.C. § 78(n) (1977), has not been definitively determined. *See* Piper v. Chris-Craft Indus., Inc., 425 U.S. 910 (1977) and the case it overruled on other grounds, Chris-Craft Indus., Inc. v. Bangor Punta, 480 F.2d 341 (2d Cir. 1973).

[30] The Commission made it clear that it was not at this time deciding whether whistle-blowing would be required: "This case does not involve, nor do we here deal with, the additional question of when a lawyer, aware of his client's *intention* to commit fraud or an illegal act, has a professional duty to disclose that fact either publicly or to an affected third party." *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,173 n.78 (emphasis added). The Commission did suggest, however, that "other existing standards of professional conduct" might require whistle-blowing. *Id.* The Commission cited as an example DR 7-102(B) of the ABA Code of

National Telephone Company, Inc. (National) leased sophisticated telephone equipment systems to commercial customers and exhibited an impressive growth rate.[31] National incurred the bulk of its expenses, including equipment, marketing, and installation costs, well before it realized any income from rental payments. Therefore, the company's cash-flow situation worsened with each new transaction.[32] By 1974, continued growth could only occur through extensive external financing. A consortium of five banks agreed to lend National a total of $21 million.[33]

In view of National's strained financial condition, however, they insisted upon the proviso that the final $2 million of the loan package would only become available upon the execution of a special Lease Maintenance Plan (LMP), which would drastically convert National from a fast-growing, highly expanding corporation to essentially a non-growth, maintenance company.[34] The LMP would be triggered

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Professional Responsibility. [Current] FED. SEC. L. REV. (CCH) ¶ 82,847, at 84,173 n.78. Although this disciplinary rule does have a whistle-blowing requirement, it does not deal with the *intention* to commit fraud but with *past* acts of a client: "A lawyer who receives information clearly establishing that . . . [h]is client *has* . . . *perpetrated* a fraud . . . shall reveal the fraud to the affected person or tribunal. . . ." ABA CODE OF PROFESSIONAL RESPONSIBILITY, Canon 7, DR 7-102(B)(1) (1977) (emphasis added). Moreover, the final clause of the disciplinary rule provides an important exception to the whistle-blowing requirement "when the information is protected as a privileged communication." *Id.* Under certain circumstances this clause may in effect "prevent the lawyer from making the disclosures required by DR 7-102(B)." *The Code of Professional Responsibility and the Responsibility of Lawyers Engaged in Securities Law Practice—A Report by the Committee on Counsel Responsibility and Liability*, 30 BUS. LAW. 1289, 1296 (1975) [hereinafter cited as *Report by Committee on Counsel Responsibility and Liability*].

DR 4-101(C)(3) of the ABA Code of Professional Responsibility addresses a client's *intention* to commit an illegal act. In such a situation the rule does not mandate disclosure but leaves it up to the attorney's discretion: "A lawyer *may* reveal . . . [t]he intention of his client to commit a crime. . . . " ABA CODE OF PROFESSIONAL RESPONSIBILITY, Canon 4, DR 4-101(C)(3) (1977) (emphasis added). For a general discussion of the issues raised by these disciplinary rules, see Hoffman, *On Learning of a Corporate Client's Crime or Fraud—The Lawyer's Dilemma*, 33 BUS. LAW. 1389 (1978); *Report by Committee on Counsel Responsibility and Liability, supra.* Hoffman takes the position that in certain circumstances the term "may" in DR 4-101(C)(3) should be interpreted to mean "must," thereby requiring whistle-blowing. Hoffman, *supra* at 1410. *See* ABA COMM. ON PROFESSIONAL ETHICS, OPINIONS, No. 314 (1965).

[31] *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,151.

[32] *Id.*

[33] *Id.* at 84,159. The five banks in the consortium were: Bankers Trust Company of New York; Mellon Bank N.A. of Pittsburgh; Central National Bank of Cleveland; The Connecticut Bank & Trust Company; and the Hartford National Bank & Trust Company of Hartford, Connecticut. *Id.* at 84,160. Of the $21 million loan, approximately $16.5 million, was used to repay short-term loans to the very same lending banks. *Id.* at 84,159-60.

[34] *Id.* at 84,158-59. The Commission pointed out that "one expert . . . testified that the LMP was 'a sort of holding pattern short of bankruptcy or levy action by the creditors.' The LMP required National to terminate all sales activities, dismiss all sales personnel and limit its operation to those necessary to service existing leases." *Id.*

when National either attempted to borrow part or all of the final $2 million or failed to meet a specified liquidity test.[35] Once having borrowed the final amount, moreover, National could only use it to change its character from a growth to a non-growth enterprise, as mandated by the LMP.[36]

Because the majority of the loan was used to pay existing debts,[37] National was in need of additional external financing. From mid-1974 to mid-1975 National was not successful in obtaining the needed financing,[38] and thus the likelihood of implementation of the LMP increased. Nonetheless, National's management, and in particular its chief executive officer Sheldon L. Hart, persisted in not disclosing the full terms of the LMP[39] in its filings with the Commission,[40] and issued optimistic letters to its shareholders[41] as well as a very encouraging press release.[42] Thus National's true economic position continued to be withheld from the public.[43]

William R. Carter and Charles J. Johnson, Jr., partners in the law firm of Brown, Wood, Ivey, Mitchell & Petty, rendered legal services to National during 1974 and 1975.[44] The Commission re-

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[35] *Id.* at 84,158.

[36] *Id.* at 84,159.

[37] *See id.* at 84,158.

[38] *Id.* at 84,154, 84,157. National explored several alternatives, namely, a proposed public offering of common stock which never materialized due to "the deteriorating public equity markets of the day," *id.* at 84,154, a sale of $1 million worth of common stock to one of its suppliers, *id.* at 84,157, the establishment of a regional bank program through which local banks would provide financing secured by new equipment leases, and a possible public offering of its debentures. *Id.*

[39] Disclosure was important, for the Commission pointed out that "[a]ll the witnesses speaking to the question agreed that the term 'lease maintenance plan' had no generally accepted meaning in the industry and that they had never used or heard that term before." *Id.* at 84,158.

[40] *Id.* at 84,158, 84,160, 84,162. The filings included a quarterly report "for the second fiscal quarter ended September 30, 1974" filed in December 1974, *id.* at 84,158, a Form 8-K current report covering the month of December 1974, which was filed on January 9, 1975, *id.* at 84,160, and an amendment to the Form 8-K current report for December 1974, which was filed on April 21, 1975. *Id.* at 84,162.

[41] *Id.* at 84,155, 84,156, 84,160. The first was issued on or about June 18, 1974 in which a 3% stock dividend was announced. *Id.* at 84,155. The remaining stockholder letters were issued on August 19 (declaring two more 1% stock dividends), *id.*; on September 12 (stating that "August had been 'an outstanding month' "), *id.* at 84,156; and on December 23 (indicating that National "was stronger now than ever before in its history"). *Id.* at 84,160.

[42] *Id.* at 84,156. The press release was issued on October 17, 1974. *Id.*

[43] *Id.* When public disclosure of National's financial crisis was ultimately made in May 1975 the market for the company's stock plumeted and bankruptcy proceedings were initiated several months later. *Id.* at 84,164.

[44] *Id.* at 84,152-53. An associate of the firm, Kenneth M. Socha, also worked with Carter and Johnson in all the matters addressed in the proceeding but he was not named as a respondent. *Id.* at 84,152 & n.31. The services included, *inter alia*, "the preparation of a form S-8 registration statement, proxy materials, other SEC filings, press releases and communications to National's stockholders." *Id.* at 84,153.

viewed their activities during the period of National's uncertain financial future. In its detailed chronological presentation of the events from May 1974 to May 1975, the Commission emphasized that despite the attorneys' actual and inferred knowledge regarding Hart's unwillingness to comply with the disclosure requirements of the securities laws and the widening gap between the company's actual financial condition and its public posture, the attorneys took little or no effective action to insure that Hart satisfied statutory disclosure requirements.[45] When National failed to issue a more candid and objective stockholder letter neither Carter nor Johnson pursued the matter.[46] Also, they did not discuss with National the disclosure deficiencies of a quarterly report issued by National even though they had an opportunity to review a draft prior to its release.[47] Furthermore, Carter did not discuss the precise effects of the LMP in a press release he drafted which announced the closing of the loan agreement between National and the five banks.[48] Finally, when an opportunity arose to advise Hart to publicize the terms of the LMP, Carter instead provided advice which allowed Hart to avoid its publication.[49] The advice resulted in a current report being filed with the Commission, which Carter had full responsibility for preparing and which did not discuss clearly the potential impact of the LMP.[50] In particular, the report failed to reveal that implementation of the LMP would abruptly change National from a growth to a non-growth company.[51]

The Commission pointed out that even after Carter and Johnson's firm was notified by the bank's counsel[52] that the LMP had been triggered, Carter and Johnson did not persist in verifying this occur-

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[45] *Id.* at 84,153-64.

[46] *Id.* at 84,157.

[47] *Id.* at 84,158. The report was filed in December 1974. *See* note 39 *supra.*

[48] *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,160. The Commission emphasized that:

> [T]he press release did not discuss either of the following matters, each of which was then within the knowledge of Carter and Johnson.
>
> (1) The precise nature and effects on National's business of the LMP and the likelihood that National would be required to implement the LMP within a short period of time; and
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> (2) The substantial limitations placed on National's operations by the [loan agreement].

Id.

[49] *Id.* at 84,159. If the LMP was an exhibit to the loan agreement, filing of the LMP with the Commission would be required. However, Carter advised that if instead the LMP was merely referred to, filing would not be necessary and publication would be avoided. Hart then did not include the LMP as an exhibit. *Id.*

[50] *Id.* at 84,160-61. This was a Form 8-K current report filed on January 9, 1975. *See* note 40 *supra.*

[51] *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,158-59.

[52] *Id.* at 84,161.

rence, even though Carter admitted that a triggering of the LMP was clearly a material event requiring disclosure.[53] Subsequent to this, moreover, Carter participated in another filing with the Commission which contained no discussion of the LMP and its effects.[54]

Carter and Johnson eventually met with Hart and strongly counseled that disclosure of the triggering of the LMP was immediately required.[55] Not only did Hart fail to heed this advice, but he attempted to have Johnson render a legal opinion for the lending banks to the effect that disclosure was not required.[56] Johnson would not issue such an opinion.[57] Furthermore, Johnson had a proposed disclosure document drafted for inclusion in National's next filing with the Commission. When National did not issue the disclosure document, however, neither Carter nor Johnson pursued this matter.[58]

An administrative law judge found the activities of Carter and Johnson sufficient to qualify as willful aiding and abetting under rule 2(e)(iii) of the SEC's Rules of Practice, and as unethical and improper professional conduct under rule 2(e)(ii).[59] Accordingly, Carter and Johnson were suspended from practicing or appearing before the Commission for one year and nine months, respectively.[60] On appeal, the Commission, after concluding that it possesses the requisite jurisdictional grant of authority to promulgate and apply rule 2(e),[61]

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[53] *Id.* at 84,162.

[54] *Id.* This was an amendment to the Form 8-K current report; the amendment was filed on April 21, 1975. *See* note 40 *supra.*

[55] *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,162.

[56] *Id.* at 84,162-63.

[57] *Id.*

[58] *Id.* at 84,163.

[59] *Id.* at 84,146, 84,164 n.1. Carter and Johnson were found to have aided and abetted violations of section 10(b) (catchall antifraud provision making it unlawful in connection with sale or purchase of any security to employ any deceptive or manipulative devise in violation of Commission rules promulgated under section 10(b)) and section 13(a) (requires filing of periodic reports with Commission, such as annual and quarterly reports) of the Securities Exchange Act of 1934, and rules 10b-5 (catchall antifraud rule promulgated under section 10(b)), 12b-20 (requires inclusion of all material information, even if not expressly asked for, in filings with Commission), and 13a-11 (requires filing of current reports with Commission) promulgated thereunder. *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,146, 84,164 n.1.

[60] *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,146, 84,164 n.1. The administrative law judge reached his conclusions using the "clear and convincing evidence standard." *Id.* at 84,146 n.3. Shortly before the Commission's decision was issued, the Supreme Court held in Steadman v. SEC, 101 S. Ct. 999, 1008-09 (1981), that in administrative proceedings the standard of proof is a "preponderance of the evidence" standard. *Id.* The Commission concluded that its decision in this matter would be the same under either standard. *Id.*

[61] *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,147. Carter and Johnson raised four major grounds in challenging the Commission's authority to promulgate rule 2(e):

> 1. The Commission was not given the express authority to adopt Rule 2(e) and in the comprehensive scheme of the federal securities law it is inappropriate to imply a power not expressly given.

reversed both findings.[62] The Commission did, however, comment that the conduct of Carter and Johnson raised serious concerns about the obligations of securities attorneys rendering disclosure advice.[63]

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2. The Administrative Practice Act, 5 U.S.C. 500, precludes the adoption or exercise of powers under Rule 2(e) because that amounts to a *de facto* establishment of a specialized SEC bar, which is expressly forbidden by the statute.

3. As a matter of policy, it is inappropriate for an agency with prosecutorial responsibilities to exercise disciplinary authority over counsel who renders advice to regulated entities.

4. The implications of the Commission's exercise of authority under Rule 2(e) are so vast that it effectively regulates the relationship between a lawyer and his client, the public and the government; and, as an administrative body with expertise in a particular area, the Commission has neither the wisdom nor the mandate to engage in such regulation.

Id. at 84,146-47. The Commission considered and rejected each of these arguments. *Id.* at 84,147-49. As to a lack of authority to adopt rule 2(e), the Commission emphasized that of the numerous courts which have considered the question, none have ruled that the Commission did not have the requisite authority. *Id.* at 84,147. It is important to note, however, that it was only recently, in Touche Ross v. SEC, 609 F.2d 570 (2d Cir. 1979), that a court for the first time directly validated the statutory authority of the Commission to adopt rule 2(e). *See* Note, *supra* note 10.

In discussing the Administrative Practice Act, 15 U.S.C. §§ 500-576 (1970), the Commission considered the purpose of the Act, which was viewed to be the elimination of "agency-established admission requirements," and its legislative history, which, according to the Commission, "makes clear that Congress . . . did not intend . . . to affect or delimit the existing disciplinary authority of federal agencies." *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,148.

The Commission recognized the potential for abuse that can occur when an administrative agency with prosecutorial responsibilities has disciplinary power over the attorneys appearing before it. *Id.* In the light of the need to preserve the integrity of its processes and the "substantial internal safeguards" which it has established, the Commission reasoned that it has an obligation to use rule 2(e) in appropriate circumstances. *Id.* *See In re* Keating, Meuthing & Klekamp, SEC Release No. 15982 (July 2, 1979) [1979 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 82,124, at 81,991-92 (Williams, Chairman, concurring). *But see id.* at 81,993-95 (Karmel, Comm'r, dissenting).

Finally, the Commission concluded that the subject area of the instant case—the performance by securities lawyers of "disclosure-related professional services"—is an area within its responsibility and expertise. *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,148-49. *See* notes 10-13 *supra* and accompanying text.

[62] *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,173. In reversing the finding that Carter and Johnson willfully aided and abetted violations of the securities laws, the Commission set out the three elements it deems necessary for liability as an aider and abettor: "1. there exists an independent securities law violation committed by some other party; 2. the aider and abettor knowingly and substantially assisted the conduct that constitutes the violation; and 3. the aider and abettor was aware or knew that his role was part of an activity that was improper or illegal." *Id.* at 84,166. *See* Woodward v. Metro Bank of Dallas, 522 F.2d 84, 94-95 (5th Cir. 1975); SEC v. Coffey, 493 F.2d 1304, 1316 (6th Cir. 1974), *cert. denied*, 420 U.S. 908 (1975). For an excellent discussion of aiding and abetting liability in securities cases see Ruder, *Multiple Defendants in Securities Law Fraud Cases: Aiding and Abetting, Conspiracy, In Pari Delicto, Indemnification, and Contribution*, 120 U. PA. L. REV. 597, 621-44 (1972).

The Commission found that Carter's and Johnson's activities easily satisfied the first two elements of the test for aiding and abetting. *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,166. In applying the third element to the instant facts, the Commission focused on the December press release redrafted by Carter and the January Commission filing prepared by

In reversing the administrative law judge's finding that Carter and Johnson had engaged in unethical and unprofessional conduct, the Commission agreed with the contention that it would be unfair to retroactively impose new rules of conduct.[64] The Commission, on the other hand, did hold that it is reasonable to require professionals practicing before it to satisfy "generally recognized norms of professional conduct, whether or not such norms had previously been explicitly adopted or endorsed."[65] The Commission reasoned, however, that securities lawyers cannot be held to generally recognized norms in situations where an attorney learns that his client is violating the securities laws since such norms have not been unambiguously established.[66] In the future there will be considerably less uncertainty,

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Carter, *see* notes 49 & 50 *supra* and accompanying text, as well as Carter's and Johnson's inaction and silence with regard to National's noncompliance with the disclosure requirements of the securities laws. *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,167-69. The Commission held that, in the absence of direct evidence of Carter's awareness that the details of the LMP were material, the evidence was not sufficient to support the conclusion that Carter was a willful aider and abettor because of his participation in the press release and Commission filing. *Id.* at 84,168. Furthermore, the record of Carter's and Johnson's silence and inaction was especially inadequate to establish liability since a higher level of intent is required in such circumstances. *Id.* at 84,168-69. *See* Rochez Bros. Inc. v. Rhodes, 527 F.2d 880, 889 (3d Cir. 1975) (deliberate intent to assist illegal conduct by silence or inaction required); Strong v. France, 474 F.2d 747, 752 (9th Cir. 1973) (for silence or inaction to be wrongful, duty to aid or disclose required).

Commissioner Evans vigorously disagreed with the majority's finding on Carter's liability with respect to the press release and Commission filing, arguing that the facts were clearly sufficient to "demand" the inference that Carter had the requisite mental state to be liable as an aider and abettor. *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,174 (Evans, Comm'r, concurring and dissenting). The Commissioner found "most troubling" the reluctance to draw "reasonable inferences" regarding Carter's "culpable mental state." *Id.*

[63] *Id.* at 84,170.

[64] *Id.* at 84,169-70.

[65] *Id.* at 84,170. The Commission cited as an example of such a generally recognized norm DR 6-101 of the ABA Code of Professional Responsibility, *id.* at 84,170 n.64, which prescribes that "[a] lawyer shall not . . . [h]andle a legal matter . . . that he is not competent to handle . . . [or] without preparation adequate in the circumstances . . . [or] neglect a legal matter entrusted to him." ABA CODE OF PROFESSIONAL RESPONSIBILITY, Canon 6, DR 6-101(A)(1)-(3) (1977) (emphasis added).

[66] *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,170. The Commission did discuss two ABA disciplinary rules which it believed "to be of such a fundamental nature that [it] would not hesitate to hold that their coverage plainly falls within the area of conduct prohibited by Rule 2(e)(1)(ii)." *Id.* at 84,170 n.65. The Code of Professional Responsibility states that "[a] lawyer shall not . . . [e]ngage in illegal conduct involving dishonesty, fraud, deceit, or misrepresentation." ABA CODE OF PROFESSIONAL RESPONSIBILITY, Canon 1, DR 1-102(A)(4) (1977). It also provides that "a lawyer shall not . . . [c]ounsel or assist his client in conduct that the lawyer knows to be illegal or fraudulent." *Id.* DR 7-102(A)(7). The Commission decided not to apply these rules in the instant proceeding for two reasons:

> First, it is unclear whether the operative terms used in these Disciplinary Rules are coextensive with the use of such terms in the statutory prohibition of Section 10(b) of the Exchange Act. Second, it is not apparent that the reach of ABA DR 1-102(A)(4)

though not total clarity, since the Commission promulgated a standard for professional conduct in its opinion.

Beginning with what it characterized as "considerable acceptance" of the principle that the discharge of professional responsibilities requires that an attorney make all reasonable efforts to persuade a client to adhere to legal mandates,[67] the Commission set out its standard for ethical and proper professional conduct, containing four major elements:

> When a lawyer [1] with *significant responsibilities* in the effectuation of a company's compliance with the disclosure requirements of the federal securities laws [2] *becomes aware* [3] that his client is engaged in a *substantial and continuing failure* to satisfy those disclosure requirements, [4] his continued participation violates professional standards unless he *takes prompt steps* to end the client's noncompliance.[68]

Although the standard applied only to lawyers with *significant responsibilities*,[69] the Commission included in this group all securities lawyers who actively participate in a company's ongoing disclosure program,[70] thus making this a very broad category. The basis for such an all-encompassing categorization is the Commission's view that such attorneys are "often involved on an intimate, day-to-day basis in the judgments that determine what will be disclosed and what will be withheld from the public markets."[71] This same viewpoint also underlies the Commission's reasoning that "[w]hen a lawyer serving in such a capacity concludes that his client's disclosures are not adequate to comply with the law . . . he is 'aware,' in a literal sense, of a continuing violation of the securities laws."[72]

The Commission emphasized that the standard primarily applies only when there is a *substantial and continuing* noncompliance with disclosure requirements and does not apply to every isolated act which the attorney believes to be a failure to comply.[73] The Commission

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> or 7-102(A)(7) is greater or any different from the reach of Rule 2(e)(1)(ii) in the case of a lawyer who willfully aids and abets a violation of Section 10(b).

In re Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,170 n.65. *See* note 30 *supra*. *But see* Okin, *Responsibilities of Corporate Counsel to Third Parties*, 54 CONN. B. J. 291, 294 (1980), where the author discusses the first level decision on Carter's and Johnson's activities and concludes that "[e]ven on the most restricted reading of the present Code of Professional Responsibility . . . Carter and Johnson surely had an obligation to do more than they did." *Id.*

[67] *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,170.

[68] *Id.* at 84,172 (emphasis added).

[69] *Id.*

[70] *Id.* at 84,171.

[71] *Id.*

[72] *Id.*

[73] *Id.* at 84,172.

hastened to add, however, that even isolated disclosure failures are not precluded if they "are so serious that their correction becomes a matter of primary professional concern."[74]

What is likely to be considered the most controversial aspect of the standard is the requirement that securities lawyers take prompt action to end the noncompliance of the client.[75] It is important to understand that the underlying premise for the prompt action requirement is the Commission's proposition that the client is the entity, that is, the corporation itself is the client, and not the management or other individuals associated with the corporation.[76] Proceeding from this perspective, the Commission listed several "suggested" affirmative steps for securities lawyers. When faced with a non-complying management the attorney is advised to consider: a direct approach to either the full board of directors or one or more individual directors or officers; procurement of the assistance of other members of the management; or resignation.[77] Furthermore, the Commission indicated

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[74] *Id.*

[75] *Id.*

[76] *Id.* at 84,171. The ABA Code of Professional Responsibility similarly provides: "A lawyer employed or retained by a corporation or similar entity owes his allegiance to the entity and not to a stockholder, director, officer, employee, representative, or other person connected with the entity." ABA CODE OF PROFESSIONAL RESPONSIBILITY, Canon 5, EC 5-18 (1977). *See* Lane v. Chowning, 610 F.2d 1385 (8th Cir. 1979), where the court held that "attorneys representing a corporation serve in the same fiduciary capacity as the directors." *Id.* at 1389.

Rule 1.13 of the proposed Model Rules of Professional Conduct makes the point clearer: "A lawyer employed or retained by an organization represents the organization *as distinct from* its directors, officers, employees, members, shareholders, or other constituents." ABA COMM. ON EVALUATION OF PROFESSIONAL STANDARDS, MODEL RULES OF PROFESSIONAL CONDUCT, rule 1.13 (1980) (Discussion draft), *reprinted in* 48 U.S.L.W. 1 (Feb. 19, 1980) (special edition) (emphasis added) [hereinafter cited as PROPOSED MODEL RULES OF PROFESSIONAL CONDUCT]. The proposed rule 1.13 has been the focus of much commentary. For favorable comments, see Kutak, *The Next Step in Legal Ethics: Some Observations About the Proposed Model Rules of Professional Conduct*, 30 CATH. U. L. REV. 1 (1980); Redlick, *Disclosure Provisions of the Model Rules of Professional Conduct*, 1980 ABF RES. J. 981 (1980). For critical remarks, see Elliot, *The Proposed Model Rules of Professional Conduct: Invention Not Mothered by Necessity?*, 54 CONN. B. J. 265 (1980); Okin, *Responsibilities of Corporate Counsel to Third Parties*, 54 CONN. B. J. 291 (1980).

[77] *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,172. Rule 1.13(c) of the Proposed Rules of Professional Conduct goes even further; it has a whistle-blowing feature that allows an attorney under certain circumstances to disclose clients' confidences. PROPOSED MODEL RULES OF PROFESSIONAL CONDUCT, *supra* note 76, at rule 1.13(c). The thrust of rule 1.13, as well as a succinct summary thereof, is found in Patterson, *An Analysis of the Proposed Model Rules of Professional Conduct*, 31 MERCER L. REV. 645, 660-61 (1980):

> The lawyer's problem is to determine what to do if his fellow agents engage in unlawful conduct which is likely to result in significant harm to the organization. Rule 1.13 recognizes the authority, indeed, the duty, of the lawyer to take appropriate measure [*sic*] to prevent the harm. Thus, if the lawyer knows that a person associated with the organization is engaged in illegal conduct which is likely to result in significant harm to the organization, the lawyer *must use reasonable efforts to*

that resignation should really be left as a last resort since "[p]remature resignation serves neither the end of an effective lawyer-client relationship nor, in most cases, the effective administration of the securities laws."[78]

The Commission stressed, however, that once an attorney passes the "critical juncture" where he concludes that his client is not heeding his advice and has embarked upon a course of continuing noncompliance,[79] "[w]hat is required . . . is some prompt action that leads to the conclusion that the lawyer is engaged in efforts to correct the underlying problem, rather than having capitulated to the desires of a strong-willed, but misguided client."[80]

The Commission did not specifically define what constitutes "prompt action," and merely indicated that it would depend in each case on the situation facing the lawyer.[81] Likewise, after stating that the attorneys' efforts to have the client comply need not necessarily be successful,[82] the Commission failed to give any specific criteria for judging the acceptability of an attorney's action. Rather, the Commission posited that the actions "must be considered in the light of all relevant surrounding circumstances,"[83] and set out a broad guideline encompassing both a good faith test and a reasonable efforts criterion: "[s]o long as a lawyer is acting in good faith and exerting reasonable efforts to prevent violations of the law by his client, his professional obligations have been met."[84]

Viewing the activities of National's management as an attempt to pervert the normal lawyer-client relationship,[85] the Commission

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> *prevent the harm* . . . . The measures taken must be designed to minimize disruption and the risk of disclosing confidences. These measures may include asking for reconsideration of the matter, [Rule 1.13(b)(1)], seeking a separate legal opinion for presentation to the appropriate authority in the organization [1.13(b)(2)], and referring the matter to the highest authority which can act for the organization [1.13(b)(3)]. If these measures fail, the lawyer *may take further remedial action*, including the disclosure of confidences to the extent necessary, if the lawyer reasonably believes that action is in the best interests of the organization [1.13(c)].

Id. (emphasis added). Thus, the disclosure of client confidences is a last resort. It should be noted that rule 1.13 does not offer the alternative of resignation, unless the term "further remedial action" of 1.13(c) is meant to include such a course of action. But such a construction would only be consistent with the thrust of rule 1.13 if resignation was indeed a "remedial action," that is, likely to be viewed as a reasonable effort to prevent the harm. *See* note 76 *supra*.

[78] *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,172.

[79] *Id.*

[80] *Id.*

[81] *Id.* at 84,172 n.77.

[82] *Id.*

[83] *Id.*

[84] *Id.* at 84,172-73.

[85] *Id.* at 84,172.

strongly implied that Carter and Johnson did not meet its newly promulgated standard since an attorney must "do . . . more than stubbornly continue to suggest disclosure when he knows his suggestions are falling on deaf ears."[86] Having decided to apply its standard only prospectively,[87] however, the Commission did not hold Carter and Johnson liable;[88] but the Commission did give notice to all securities lawyers that it will apply the standard to all future proceedings where a violation of subparagraph (ii) of rule 2(e)(1) is alleged.[89]

The standard presented by the Commission[90] is certainly consistent with its modern philosophy of relying on the securities bar to, in effect, be its police force.[91] Critics of this practice emphasize that it will deter corporate executives from presenting problems to an attorney[92] and will cause securities lawyers to become overly concerned with their own potential liabilities, thereby resulting in a lack of zealous representation of their corporate clients.[93] At the heart of the controversy lies the grave concern over the prior attempts by the Commission to impose a whistle-blowing requirement.[94] By not including this requirement in its standard,[95] the Commission reduces the

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[86] *Id.*

[87] *Id.* at 84,146.

[88] *Id.* at 84,173.

[89] *Id.*

[90] *Id.* at 84,172. It is not totally clear why the Commission felt it necessary to promulgate the standard in an administrative proceeding. As the dissent astutely pointed out, such a course of action denied prior input not only to the public, but also to key personnel within the Commission, such as its General Counsel and operating division. *Id.* at 84,177-78 (Evans, Comm'r, concurring and dissenting). Although the Commission did state that it would issue a subsequent release in which comments from the public would be solicited. *Id.* at 84,170, there seems to be no convincing justification for not using such a release as a first step rather than as an afterthought.

[91] *See* note 11 *supra*. As former Commissioner Sommer remarked in a widely publicized speech: "the attorney will have to function in a manner more akin to that of the auditor than to that of the advocate." Sommer, *The Emerging Responsibilities of the Securities Lawyer* [1973-1974 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 79,631, at 83,689 (Jan. 1974).

[92] *See* Elliot, *supra* note 76, at 276; Lowenfels, *supra* note 11, at 435.

[93] *See* Johnson, *supra* note 10, at 660.

[94] *See* text accompanying notes 17-20 *supra*. For example, one commentator, after stressing that lawyers are fiduciaries of their clients, went on to caution that "[t]he Commission's effort to substitute itself, or the public, as the lawyer's true client would prevent the profession from acting as it is expected to and would thereby undermine the influence of lawyers on their clients and in the long run would discredit the disclosure process itself." Cooney, *The Registration Process: The Role of the Lawyer in Disclosure*, 33 BUS. LAW. 1329, 1334 (1978).

[95] National had a number of outside directors who had the potential to, and ultimately did, take effective action to make the necessary statutory disclosure. *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, at 84,164. Whether the standard will also apply to situations where no independent board exists is not totally ascertainable from the Commission's opinion. The inclusion, however, of resignation as the final course of action by an attorney, *id.* at 84,172, suggests that the standard will have universal application.

scope of the controversy to the narrower issue of whether securities lawyers, in addition to the requisite ethical responsibilities for ensuring that a client complies with legal mandates,[96] ought to be subject to a separate Commission standard as well. In light of the importance of the disclosure requirements of the Securities and Exchange Acts of 1933[97] and 1934,[98] duly recognized by the judiciary,[99] and the Commission's admission that it is unable, on its own, to adequately monitor compliance with the disclosure requirements,[100] the placing of a reasonable duty on securities lawyers does not seem overly burdensome or likely to disrupt the attorney-client relationship. The key inquiry is whether the standard set forth is indeed reasonable, for if it proves not to be it could cause a degree of disruption that might ultimately impair the disclosure process.

The Commission's standard[101] is well-reasoned and does not place an unfair burden on securities lawyers. Although it is designed to bring many practicing securities lawyers within its application,[102] it is generally limited to situations where an attorney knows that his client is engaged in a substantial and continuing failure to make the proper disclosures,[103] which was clearly the situation in the instant case.[104] As for the degree of knowledge that will be required to satisfy the awareness element of the standard, the Commission has not directly addressed this issue. The Commission's high threshold requirement to infer knowledge for aiding and abetting liability,[105] however, especially when silence or inaction are involved,[106] is indicative that a similarly high criterion will be used to determine whether the knowledge requirement of its ethical standard has been satisfied.

The burden of establishing that some prompt action has been taken should not prove to be a difficult undertaking. An attorney will usually keep copies of memoranda in which he counsels the degree of disclosure necessary for statutory compliance, as well as drafts of

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[96] *See* notes 30, 66, 67 & 76 *supra* and accompanying text.

[97] Sections 1-328 of the Securities Act of 1933, 15 U.S.C. §§ 77a-77bbb (1977).

[98] Sections 1-35 of the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78kk (1977).

[99] *See* Hochfelder, 425 U.S. at 195; SEC v. Capital Gains Research Bureau, 375 U.S. 180, 197-99 (1963).

[100] *See* note 11 *supra*.

[101] *See* text accompanying note 68 *supra*.

[102] *See* text accompanying notes 69-71 *supra*.

[103] *See* text accompanying note 68 *supra*.

[104] *See* text accompanying notes 44-58 *supra*. Had the Commission's standard already been in effect, Carter and Johnson would have likely been found liable. *See* text accompanying notes 85-86 *supra*.

[105] *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, 84,167. *See* note 62 *supra*.

[106] *In re* Carter, [Current] FED. SEC. L. REP. (CCH) ¶ 82,847, 84,169. *See* note 62 *supra*.

disclosure documents he has prepared. A series of such memoranda addressed to the appropriate people in the chain of command of the client system, up to and including the board of directors, should be more than adequate to satisfy the good-faith test[107] which the Commission established. There is some uncertainty in this area, however, since the Commission did not define what it means by "prompt action," an omission which the securities bar is certain to consider material. In making its good-faith test very liberal,[108] the Commission does offer some comfort to securities lawyers.

The Commission appropriately has stressed that an attorney's resignation should be considered only as a last resort.[109] Resignation is a more powerful device than most attorneys realize[110] since it may well lead to statutory compliance by the client. The decision to resign should only be reached after a careful consideration of its negative impact on the client and a balancing of the weight of the conflicting effects. To do less would be unethical since a lawyer "owes his allegiance" to his client.[111]

The definition of the client as the corporate entity,[112] and the confinement of the standard to activities within the client system,[113] avoid the complex issues which arise when disclosures violate client confidences.[114] Furthermore, the definition of client is consistent with the American Bar Association Code of Professional Responsibility, which states that "[a] lawyer employed or retained by a corporation or similar entity owes his allegiance to the entity."[115] The entire standard, moreover, complements the duties that the Code of Professional Responsibility presently impose: a lawyer is prohibited from engaging in fraud[116] or from assisting his client in behavior "that the

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[107] *See* text accompanying note 84 *supra*.

[108] *See* text accompanying note 84 *supra*.

[109] *See* text accompanying note 78 *supra*.

[110] As one commentator pointed out:

> Directors will rarely act contrary to firm legal advice, and they will certainly think again if their lawyers show a willingness to resign when their advice is declined. They will think again not only because of the potential public consequences if the resignation becomes generally known, but also because most managements genuinely respect the judgment and character of their counsel, and are bound to be impressed by the courage and conviction that a decision to resign involves.

Cutler, *The Role of the Private Law Firm*, 33 Bus. Law. 1549, 1557 (1978).

[111] *See* note 76 *supra*.

[112] *In re* Carter, [Current] Fed. Sec. L. Rep. (CCH) ¶ 82,847, at 84,171. *See* note 76 *supra* and accompanying text.

[113] *In re* Carter, [Current] Fed. Sec. L. Rep. (CCH) ¶ 82,847, at 84,172. *See* note 77 *supra* and accompanying text.

[114] *See* notes 76 & 77 *supra*. *But see* Elliot, *supra* note 76, at 276-77.

[115] ABA Code of Professional Responsibility, Canon 3, EC 5-18 (1977). *See* note 76 *supra*.

[116] *See* ABA Code of Professional Responsibility, Canon 1, DR 1-102(A)(4) (1977); note 66 *supra*.

lawyer knows to be illegal or fraudulent;"[117] "[a] lawyer may reveal . . . [t]he intention of his client to commit a crime;"[118] and a lawyer is required to disclose non-privileged information "clearly establishing that . . . [h]is client has . . . perpetrated a fraud."[119] Also, the standard parallels rule 1.13 of the Proposed Model Rules of Professional Conduct,[120] although it does not go as far as rule 1.13,[121] which allows the disclosure of client confidences when there is a clear "violation of law [which] . . . is likely to result in substantial injury to the organization."[122]

In conclusion, the ethical standard enacted by the Commission in *In re Carter*, if judiciously applied, will not present a severe intrusion into the attorney-client relationship or present an unreasonable burden on the securities bar. The remarks of a former president of the American Bar Association perhaps best capture what can reasonably be expected of a securities lawyer:

> The lawyer representing business today, if he is to live up to his new responsibilities, will endeavor to avoid the errors of the past; he will shun advice that is motivated by a desire to preserve the rubrics of a vanished era; he will be alive to the social, economic, and political implications of the time; he will avoid a narrow, short-sighted approach to his clients' problems; he will have the courage to advise against a business program or device that, although legally defensible, is in conflict with the basic principles of ethics. Failing these, he not only will be ignoring his obligations to society but will be doing a disservice to his client. That client may find itself in the position of winning a legal battle but losing a social war.[123]

Joseph R. D'Amore

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[117] ABA CODE OF PROFESSIONAL RESPONSIBILITY, Canon 7, DR 7-102(A)(7) (1977). *See* note 66 *supra*.

[118] ABA CODE OF PROFESSIONAL RESPONSIBILITY, Canon 4, DR 4-101(C)(3) (1977).

[119] *Id.* Canon 7, DR 7-102(B)(1).

[120] PROPOSED MODEL RULES OF PROFESSIONAL CONDUCT, *supra* note 76, at rule 1.13(c).

[121] *See* note 77 *supra*.

[122] PROPOSED MODEL RULES OF PROFESSIONAL CONDUCT, *supra* note 76, at Rule 1.13(c).

[123] Gossett, *The Corporation Lawyer's Social Responsibilities*, 60 A.B.A.J. 1517, 1519 (1974).