The SEC Imposes Up-the-Ladder Reporting Duties on Corporate Attorneys

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In January 2003, the Securities and Exchange Commission (SEC) adopted rules imposing up-the-ladder reporting requirements when corporate attorneys appearing and practicing before the Commission become aware of evidence of a material violation by the company or any of its officers, directors or employees. In doing so, the Commission entered uncharted waters in what has been described as the first significant effort by Congress to mandate the federal regulation of lawyers.

Section 307 of the Sarbanes-Oxley Act directed the SEC to adopt rules 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 one of its agents to the chief legal counsel or the chief executive officer. If corporate officials do not appropriately respond, the attorney must report the evidence to the board's audit committee or to another board committee comprised solely of directors not employed directly or indirectly by the company, or to the board of directors. This mandate is within the broader statutory direction to establish minimum standards of professional conduct for attorneys appearing or practicing before the Commission in any way in the representation of public companies. Acting on the statutory mandate, the SEC has adopted a comprehensive attorney corporate reporting regime.

In mandating up-the-ladder reporting by both inside and outside corporate counsel, the SEC gave attorneys the alternative of reporting to a committee of the company's board of directors called the qualified legal compliance committee. Thus, counsel will have the choice of reporting to corporate officers or to the committee.

The SEC has also adopted broad definitions of "attorney" and "appearing and practicing" and "in the representation of an issuer." Taken collectively, these definitions recognize that attorneys interact with the Commission in a number of ways on behalf of companies, and that such conduct should be covered by the new SEC rules.

Both the Sarbanes-Oxley Act provisions and the SEC rules are based on the principle that the client of an attorney representing a company before the Commission is the company itself, and not the company's individual officers or employees that the attorney regularly interacts with and advises on the company's behalf. Those officers and other employees, like the attorney, have a fiduciary duty to act in the best interests of the company and its shareholders. ■