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Corporate Gatekeepers: An Examination of the Transactional Lawyer's Role

William H. Dorton¹

It is both our burden and our glory that we are expected to live by a high professional standard and earn a living at the same time. We do not have the luxury of the clergy who can live in the temple and condemn the market place. Nor do we have the more flexible standard of those who live solely in the market place. We have to carry the standards of the temple into the market place and practice our trade there. That is why a country which questions its moral behavior inevitably questions its lawyers.

Dean Redlich²

INTRODUCTION

Several highly public corporate scandals at the beginning of the last decade exposed a systemic problem in the priorities of a considerable number of corporate lawyers.³ Those lawyers took advantage of their positions of public trust and confidence and failed to restrain corporate insiders who were perpetrating frauds on unsuspecting shareholders.⁴ These scandals shocked the market community, which is premised on open and honest communications in transactions. Enron is the paradigmatic example. Enron's lawyers facilitated transactions that drastically misstated Enron's financial situation over the course of several years.⁵ The serious nature of such a scandal is not to be taken lightly; the revelation of the fraud put Enron and its accounting firm out of business, eliminating thousands

¹ University of Kentucky College of Law, JD expected 2011. The author would like to offer sincere thanks to Professor Rutheford B Campbell for his assistance in exploring the original topic and offering needed criticism and advice.
² Norman Redlich, Lawyers, the Temple, and the Market Place, 30 Bus. Law. (Special Issue) 65, 65 (1974).
⁵ Pollock, supra note 3.
of jobs and shaking investor confidence in the securities market. Enron's lawyers' culpable behavior has been characterized as acting as accessories to the fraudulent transactions by failing to "blow the whistle," and "back[ing] down when rebuffed" by Enron's officers. In the wake of Enron and related scandals, the corporate transactional lawyer has been placed squarely in the crosshairs of legislative and regulatory reform.

A. Informational Asymmetry and Required Disclosures

Enron and other like scandals were met with widespread public condemnation and swift legislative response largely because they shook the U.S. economic system at its roots. Since Adam Smith's seminal insights in The Wealth of Nations, most western market economies have been premised on a capital-formation process structured on individual self-interest. A fundamental precept of the market economy is that each of countless actors pursues his individual interests with access to only a tiny sliver of the information generated by the market as a whole. In doing so, the individual market actor passively invests his or her money for management by corporate insiders. While unsophisticated investors are more or less on equal footing with one another, sophisticated investors and corporate insiders have much greater access to investment information. This "informational asymmetry" tilts the playing field toward the corporate insider and creates an enormous potential for abuse. This poses a very real threat to capital formation: when the passive investor becomes uncomfortable investing in the market because of the fear of manipulation by corporate insiders, the entire system may falter for lack of funds.

The grave threat to capital formation posed by the asymmetrical flow of information requires steadfast maintenance through an efficient system of regulation. The primary means used to address this broad informational disparity between individual investors and corporate insiders has long been the type of required disclosures promulgated in the wake of the 1929 stock

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7 Pollock, supra note 3.
8 See infra Part IV for further discussion of the legislative response.
9 See Joseph Cropsey, Adam Smith, in History of Political Philosophy 635, 649 (Leo Strauss & Joseph Cropsey eds., 3d ed. 1987). Cropsey describes Smith as "an architect of our present system of society" for "his famous elaboration of the principles of free enterprise or liberal capitalism." Id. at 635.
10 See id. at 649-50.
11 Michelle M. Harner, Corporate Control and the Need for Meaningful Board Accountability, 94 MINN. L. REV. 541, 551-52 (2010).
13 Cf. id. at 152-53 (explaining that less "informational asymmetry" results in a market where investors can make more informed decisions about the value of an investment).
market crash. The Securities Act of 1933 and the Securities Exchange Act of 1934 enacted a system of comprehensive disclosure, including establishment of the Securities and Exchange Commission (SEC) as an enforcement mechanism. The rationale supporting required disclosures in the corporate context is three-fold: incentivize corporate managers to act in their shareholders' best interests, reduce informational asymmetry in the markets to facilitate efficient transactions, and maintain investor confidence in securities markets. The meaningful idea is that honest communication is fundamental to the integrity of the system as a whole.

While the SEC is generally effective in enforcing disclosure requirements, using the threat of legal action as its primary deterrent, high-profile corporate scandals involving fraudulent disclosures, like Enron, continue to occur.

B. Advent of the Gatekeeper

In an effort to fulfill its mission to ensure adequate flow of information to investors, the SEC regularly adjusts its regulatory focus to rein in conduct by corporate actors that undermines the foundation of the system. Transactional lawyers who operate in the corporate sphere are natural objects of the SEC's interest due to the integral role they play in corporate activity. Transactional lawyers' activities range from assisting in

14 Id. at 149-51.
18 Ripken, supra note 12, at 151-54.
19 See Jill E. Fisch, The Overstated Promise of Corporate Governance, 77 U. CHI. L. REV. 923, 956 (2010) (reviewing JONATHAN MACEY, CORPORATE GOVERNANCE: PROMISES KEPT; PROMISES BROKEN (2008) (noting that "accurate share prices depend on honest disclosure"); James A. Fanto, Recognizing the "Bad Barrel" in Public Business Firms: Social and Organizational Factors in Misconduct by Senior Decision-Makers, 57 BUFF. L. REV. 1, 36 (2009) ("[T]he law's focus is on accurate disclosure of material information . . ."); Hillary A. Sale, Banks: The Forgotten(?) Partners in Fraud, 73 U. CIN. L. REV. 139, 139 (2004) (characterizing disclosure as "the chief method for cleansing fraud"); see also F.A. HAYEK, THE CONSTITUTION OF LIBERTY 29 (1960). The author notes the importance of being able to act in society pursuant to one's own unique knowledge and points out the "inevitable ignorance of all of us concerning a great many of the factors on which the achievement of our ends and welfare depends." Id. (citation omitted).
21 See, e.g., Stephen M. Cutler, Director, Division of Enforcement, SEC, Address to
the structuring, negotiation, and documentation of business transactions to advising corporate directors in complying with fiduciary duties owed to shareholders. Their utility as catalysts to SEC enforcement goals has long been recognized. As early as 1973, commentators observed that corporate lawyers are essential to a corporation’s entry into transactions in securities markets. The corporate-lawyer-as-gatekeeper notion was widely adopted by courts, academics, and regulators before Enron and related corporate scandals cast such a probing light on their role.

The fraud and mismanagement that occurred to such devastating effect at Enron, and elsewhere, refocused scrutiny on the corporate transactional lawyer’s role as gatekeeper. To the consternation of legislators, regulators, and academics, a problem they had considered and addressed recurred unexpectedly in a spectacular and public fashion. As one observer noted, “[t]he frauds occurred despite several levels of monitoring by, among others, directors, prominent accounting and law firms, institutional shareholders,

the UCLA School of Law: The Themes of Sarbanes-Oxley as Reflected in the Commission’s Enforcement Program (Sept. 20, 2004), available at http://www.sec.gov/news/speech/spcho92004.htm ("Consistent with Sarbanes-Oxley’s focus on the important role of lawyers as gatekeepers, we have stepped up our scrutiny of the role of lawyers in the corporate frauds we investigate.").


23 See Marc I. Steinberg, Attorney Liability for Client Fraud, 1991 COLUM. BUS. L. REV. 1 for a pre-Enron review of cases and literature.


25 See Felts v. Nat’l Account Sys. Ass’n, Inc., 469 F. Supp. 54, 68 (N.D. Miss. 1978) (observing that, because the corporate lawyer could reasonably foresee that investors would rely on his skill, he “voluntarily assumed a relationship . . . with the purchasers of these securities”); see also Steinberg, supra note 23, at 1-2.

26 For a variety of perspectives on the transactional lawyer’s role in the “post-Enron” world, see Rutheford B Campbell, Jr. & Eugene R. Gaetke, The Ethical Obligation of Transactional Lawyers to Act as Gatekeepers, 56 RUTGERS L. REV. 9, 14 (2003) (arguing that the MODEL RULES OF PROFESSIONAL CONDUCT provide insufficient guidance to transactional lawyers); Roger C. Cramton et al., Legal and Ethical Duties of Lawyers After Sarbanes-Oxley, 49 VILL. L. REV. 725, 733 (2004) (setting out the circumstances surrounding the SEC’s new rules, examining the application of the rules, and identifying certain ambiguities in the rules); Jerry A. Eisenberg & William E. Donnelly, Lawyers as Gatekeepers: An SEC Enforcement Perspective, 39 REV. SEC. & COMMODITIES REG. 97, 97 (2006) (describing the SEC rules, the case law in which these rules were applied, and expressing certain cautions inherent in the rules); Larry E. Ribstein, Market vs. Regulatory Responses to Corporate Fraud: A Critique of the Sarbanes-Oxley Act of 2002, 28 J. CORP. L. 1, 3 (2002) (arguing that “more regulation is not the answer” because the recent “frauds occurred after seventy years of securities regulation”); Fred C. Zacharias, Coercing Clients: Can Lawyer Gatekeeper Rules Work?, 47 B.C. L. REV. 455, 455 (2006) (focusing on the incentives lawyers have to implement coercive rules relating to regulatory changes and the MODEL RULES OF PROFESSIONAL CONDUCT).
debt rating agencies, and securities analysts." A recalibration of the regulatory framework was inevitable.

C. Recalibration of the Gatekeeper Role

The response to the regulatory system's abject failure to deter massive fraud was swift and took place along three fronts: Congress addressed the failure through legislation, the SEC acted via rulemaking, and the American Bar Association (ABA) amended their rules of professional ethics. Congress acted first, passing the Sarbanes-Oxley Act in 2002 ("Sarbanes-Oxley"), which, among its sweeping reforms, directed the SEC to promulgate rules to govern corporate lawyers' responses to managerial misconduct. Congress, in Sarbanes-Oxley, mandated that the new rules require any lawyer who represents an SEC issuing company and who "pract[i]ces before the Commission" 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)." If such reporting does not elicit an "appropriate[] respon[se]" to the alleged wrongdoing, the lawyer is required "to report the evidence to the audit committee . . . or to another committee of the board of directors comprised solely of [independent] directors . . . or to the board of directors." The SEC, in response to a "tight congressional deadline," issued a new rule addressing those directives.

The ABA called its own task force to address managerial misconduct in the corporate governance arena. The task force's report addressed corporate governance in general, and in particular, Model Rule 1.6, regarding attorney-client confidentiality, and Model Rule 1.13, regarding representation of organizations. The task force considered requiring disclosures to relevant regulatory authorities in cases of managerial misconduct, but it ultimately recommended a permissive disclosure standard.

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27 Ribstein, supra note 26, at 3 (emphasis added).
28 Campbell & Gaetke, supra note 26, at 10-12.
31 Id.
32 Id. § 7245(2).
33 Campbell & Gaetke, supra note 26, at 11.
35 Cramton et al., supra note 26, at 729.
36 Id. at 729-30; see also Campbell & Gaetke, supra note 26, at 12-13.
37 See ABA, Report of the American Bar Association Task Force on Corporate Responsibility, reprinted in 59 Bus. Law. 145, 172-73 (2003); see also Cramton et al., supra note...
D. Summary of Contents

This Note will examine the debate regarding the appropriate regulatory framework to ensure corporate compliance with SEC disclosure requirements, the early precedential proceedings interpreting the SEC's new approach, and what those interpretations mean for the practicing corporate lawyer. Part I proceeds with a general primer on corporate "culture," wherein I describe the manner in which the culture of large corporate law firms drifted toward a client-driven agenda that fundamentally altered the corporate lawyer's notion as to his goals and appropriately achieving them. Part II describes the approach of the Model Rules of Professional Conduct to the gatekeeper role of the transactional lawyer. I ultimately conclude that the Model Rules as amended remain woefully inadequate to provide the proper incentives for satisfactory conduct by transactional lawyers. Part III introduces Sarbanes-Oxley and the regulatory framework promulgated under its mandate. In this section, I examine the mechanics of the regulatory approach as well as several enforcement actions brought by the SEC pursuant to its authority. I conclude that the SEC approach under Sarbanes-Oxley is superior, but flawed. One flaw is that the culpability threshold is too low, implicating corporate gatekeepers whose behavior does not warrant the accompanying sanctions. I suggest that the SEC would be a superior monitor of the securities markets if it implemented a more transparent process whereby specific types of gatekeeper conduct are identified and associated with corresponding sanctions. Finally, I argue for a two-tiered system in which different proceedings accompany different levels of culpability.

I. Prelude: Corporate Gatekeepers and Cultural Drift

A. Markets as Social Groups

Social anthropology inevitably bears on any analysis of a discrete group of people who comport themselves according to a common set of behavioral norms and beliefs. The corporate boardroom with its constituent players—directors, managers, and counsel, to name a few—provides an example of a distinct "culture" that may be fruitfully analyzed using anthropological concepts. This analysis applies equally well to the culture that attends large law firms that service corporate clients. Over the last three decades, a new set of behavioral norms and cultural notions has emerged regarding

26, at 730 n.17.
39 See McWilliams, supra note 4, at 226-27.
40 See id.
41 See id.
the proper beneficiaries of the corporate gatekeeper’s duty to ensure
the efficient operation of the financial markets.42 Large corporations and
the large law firms that counsel them effectively “instrumentalized” the
positive laws of corporations and put them to work for their financial
advantage through manipulation of financial disclosures.43 This process
developed, in large part, because counsel to large corporations capitalized
on their public reputations for honesty and fair-mindedness to assist in
structuring and documenting financial transactions.44 The culture of the
large law firm drifted from one of accountability and duty to one of self-
interested profit maximization.45

The corporation is usefully conceived of as a “little planned society,”46
an institution underpinned by cultural norms and rules. Those cultural
norms include:

- a perceived and shared understanding of a basis for trust;
- confidence in the function of agency;
- confidence in the function of contract;
- socially acceptable desire for the increase of private wealth from a passive source;
- public institutions to serve private interests;
- the concept of money;
- confidence in various means of information communication, retention and
  exchange;
- confidence in certain reliable expectations on which accurate
  prediction can be based;

More broadly, individuals who participate in the American financial
markets are a cohesive social group whose “common goals, understandings,
symbols and communication are both informed by and describe a culture.”48
A hallmark of this market-based cultural group is investor confidence. If an
investor does not feel comfortable putting his or her money into the hands
of corporate managers, the market does not function efficiently.49 Because
of its emphasis on passive investment, the integrity of the entire cultural
system requires a critical threshold of investor trust in the quality

42 See id. at 273-74 (“Over a period of some 30 years the financial markets’ guardian
professions altered the informing notion of their culture from public service to profit maxi-
mization.”).
43 Id. at 268. McWilliams describes “instrumentalization” as the process of law firms using
the “cultural values” attached to the legal profession to their advantage. Those firms were,
in turn, instrumentalized by corporate managers as part of a “power exercise in which one
social group employs leverage to obtain the agency of another. Id.
44 Id. at 261-62.
45 See id. at 228.
46 Id. at 246 (quoting RONALD H. COASE, ESSAYS ON ECONOMICS AND ECONOMISTS 8
(1994)).
47 Id. at 245.
48 Id. at 244.
49 See id. at 256 (“[T]he market rests upon a cultural notion of investor protection in ef-
ficient markets based on good faith and information symmetry.”).
of information provided by those who seek to attract investments. This is, for practical purposes, why the SEC exists: to force relevant disclosures so that ill-informed investors are able to make rational decisions with their money.

B. The "New Breed" of Corporate Executives

In the face of "[t]he huge mass of information, and the huge numbers of members of the market community who generate, manipulate, and employ it," mere SEC disclosure requirements are insufficient to ensure the systemic integrity of the market. Further muddying the waters of the market culture, scholars have noted the rise of "a new breed of corporate executives who are unconstrained by the traditional devices." The characteristics of the "new breed" of corporate manager include high tolerance for intense competition, exaggerated sense of ego and self-interest that buffers moral anxiety, a large appetite for risk-taking, and intense firm loyalty. While the prevalence and presence of corporate executives with such a personality-type has facilitated share price appreciation for particular companies, it has also facilitated the use of questionable accounting methods and legal advice to disastrous effect, namely, enhanced executive compensation and excessive risk-taking with the money of passive investors.

C. The Need for a Gatekeeper

The new breed of corporate executives, with their penchant for excessive risk-taking and disruption of the flow of accurate information to the market, needed more than mere positive regulation from Congress and the SEC to keep them from destroying the delicate balance of the market. The failure of positive rules to regulate the flow of information to financial markets—due to their rigidity—requires that cultural norms fill the void. Enter the corporate transactional lawyer: a "cultural shepherd" whose role is to steer the company toward compliance with positive regulations, even for matters only implicitly governed by those regulations. Corporate gatekeepers have been described as "reputational intermediaries who provide verification and certification services to investors." Put another

50 See id. at 248.
51 Id. at 257.
52 Ribstein, supra note 26, at 9 (citation omitted).
53 See McWilliams, supra note 4, at 249-51.
54 See id. at 248-50.
55 Id. at 256.
56 Id.
57 Id.
58 Id. at 257 (quoting Coffee, supra note 22, at 1405 (internal quotation marks omitted)).
way, the cultural role of the corporate gatekeeper is to serve as a "proxy for the eyes and ears that most investors lack, and [as] a check on issuers' opportunistic behavior." The corporate lawyer obtained this cultural role via public trust in the "civic trusteeship" nature of her profession.

D. Failure of the Gatekeeper

As the foregoing implies, Enron and like scandals demonstrated a spectacular failure of the gatekeeper professionals involved. The failure of Enron's gatekeepers demonstrates the "culture drift" that has taken place in the corporate legal profession. It amounts to a recalibration of the corporate law firm's culture from one based on service to one based on self-regard and profit. This "re-branding" was accompanied by a change in the way law firm culture operated. Senior members became valued for their relationships with corporate insiders; relationships that were leveraged to obtain work for younger partners and associates and increase the firm's bottom line. In addition to the focus on "rainmaking partners," firms began to shop among each other for clients willing to pay the highest rates. The dominance of the senior member who aligned with corporate insiders led inexorably to cultural drift inside the firm and toward alignment with the aggressive and reckless culture of the "new breed" corporate manager.

As a result, the corporate lawyer tended to "adopt the client's subjective culture, including the associated 'pathologies . . . including excessive optimism and loyalty, and reduce their concern for their . . . firm's reputation.' The result was, in socio-anthropological terms, an example of "a power exercise in which one social group employs leverage to obtain the agency of another." This "social reordering" resulted in the corporate legal profession instrumentalizing its "cultural values," that is, its reputation for trustworthiness. In short, effective gate-keeping by corporate lawyers was jettisoned in the pursuit of profit, a process facilitated by corporate law firms becoming subservient to increasingly aggressive clients.

59 Id. at 258.
60 Id. at 259 (citation omitted) (internal quotation marks omitted).
61 Id. at 262.
62 Id.
63 Id. at 264.
64 Id. at 265 (citation omitted).
65 Id. at 266.
66 Id. (first alteration in original) (quoting Ribstein, supra note 26, at 9).
67 Id. at 268.
68 See id.
II. The Model Rules of Professional Conduct's Permissive Culpability Predicate

The Introduction and Part I serve as a prelude, but the real story of the situation the modern corporate transactional lawyer finds herself in begins with the Model Rules of Professional Conduct ("Model Rules"). It is telling that the Model Rules were promulgated long before Enron and related scandals shook Congress and the SEC to action, yet they remain essentially unchanged. The corporate gatekeeper's role as "proxy for the eyes and ears that most investors lack" was well known to the Model Rules' drafters. As early as 1973, the Second Circuit observed that "[e]ffective implementation of [investor] safeguards ... depends in large measure on the members of the bar who serve in an advisory capacity to those engaged in securities transactions."

There is, however, a wide gulf between simply recognizing that an issue exists and setting forth an adequate regulatory framework within which to address the issue. The critical flaw in the approach taken by the drafters of the Model Rules is its culpability predicate: a lawyer must have actual knowledge of a violation in order to be placed under any obligation to report. The drafters' culpability requirement, though problematic, was not novel. Prior to Sarbanes-Oxley, many courts held that corporate attorneys owed no independent duty of disclosure "absent proof of the elements of principal or aiding and abetting liability."

Without positive law adopted by Congress to govern less-than-criminal behavior, the corporate lawyer's professional conduct was governed exclusively by the Model Rules. The essential thrust of the Model Rules as they concern the lawyer's gatekeeper role is contained in Model Rules 1.13 and 1.2(d). "Under Model Rule 1.13(a), an organization's lawyer is to consider her 'client' to be the organization itself." This "entity theory" provides a "crucial frame of reference" for the corporate lawyer, dictating that she does not represent any of the various corporate stakeholders individually, but the corporate entity as a whole. The entity theory is

69 Id. at 258.
71 Campbell & Gaetke, supra note 26, at 51-52 (emphasis added).
72 Steinberg, supra note 23, at 2 (citation omitted).
73 These rules are still highly relevant to the corporate lawyer's course of conduct, and will be compared with the SEC's approach in Part III.
74 Campbell & Gaetke, supra note 26, at 15-16.
75 Id. at 16 (citations omitted).
76 Id. at 16-17 (citation omitted); see also Arifin v. Matuszewich, No. 98 C 1591, 2000 U.S. Dist. LEXIS 8624, at *14-15 (N.D. Ill. June 20, 2000). But see Berliner Corcoran & Rowe, L.L.P. v. Orian, 563 F. Supp. 2d 250, 256 (D.D.C. 2008) (holding that Rule 1.13 does not presume a conflict of interest when an attorney represents both an organization and an individual employed by the organization).
useful in the abstract: counsel to the corporation simply looks to the best interests of the corporation as a whole. As a practical matter, however, the entity theory has its shortcomings. Observers have noted that the Model Rules' "blithe reference to the client's identity under the entity theory" collapses when the actions or decisions of corporate managers would injure other corporate stakeholders or constitute violations of the securities laws.77

An example of such a situation is found in the structural conflicts inherent in the makeup of the corporate entity.78 Tensions between the interests of various corporate stakeholders inevitably arise in the conduct of corporate affairs. For example, corporate lawyers are natural allies of the managers who enlist their services and bear but an abstract relationship, in most cases, with the shareholders.79 These situations can become challenging from an ethical perspective, and Model Rule 1.13(b) provides guidance. There are two essential components to the operation of Rule 1.13(b): the culpability predicate and instructions for how the lawyer should respond if that predicate is met. In situations where the lawyer "knows" that a corporate constituent "is engaged in action, intends to act or refuses to act in a matter related to the representation"80 and the constituent's action is "a violation of a legal obligation to the organization,"81 or is a "violation of law that reasonably might be imputed to the organization and that is likely to result in substantial injury to the organization,"82 the lawyer's responsibility to act is triggered. Pursuant to the foregoing analysis, the culpability predicate under the Model Rules approach is best stated as an actual knowledge requirement.

The actual knowledge standard promulgated under Model Rule 1.13(b) has been harshly criticized in the post-Enron academic literature. One hypothetical scenario demonstrating the problem posits that the president of a corporation requests that the lawyer "lend assistance to an unwarranted corporate gift to a friend of the president."83 Under the permissive Rule 1.13(b) standard, the lawyer could lend assistance, assuming the gift was not a violation of the president's fiduciary duties, and not violate the rule.84 This is true whether the lawyer's failure to inquire into the nature of the gift was negligent or even reckless.85 The conclusion is inescapable: "[s]uch a lax standard is impossible to reconcile with any claim that the legal profession requires sensible, fair, and demanding conduct from its members or that

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77 Campbell & Gaetke, supra note 26, at 21 (citation omitted).
78 Id. at 30.
79 See id.
80 MODEL RULES OF PROF'L CONDUCT R. 1.13(b) (2009).
81 Id.
82 Id.
83 Campbell & Gaetke, supra note 26, at 53.
84 Id.
85 See id. at 53-54.
members of the profession function as gatekeepers." Some observers have concluded that the “triggering standard” under the Model Rules is “so weak that lawyers inclined to do so can easily circumvent it.”

Once the corporate lawyer has actual knowledge of misconduct, the action required of her is left to her discretion under Model Rule 1.13(b). Specifically, the rule requires her to “proceed as is reasonably necessary in the best interest of the organization.” It is relevant to note that the rules were amended by the ABA in 2003—post-Enron—and yet the amended version retains the discretionary regime as to how the lawyer should proceed. The amended rules require that the lawyer “refer the matter to higher authority in the organization, including, if warranted by the circumstances to the highest authority that can act on behalf of the organization,” but this requirement does not apply if “the lawyer reasonably believes that it is not necessary in the best interest of the organization to do so.” Further, if the lawyer acts under Rule 1.13(b) but is rebuffed, the amended version of Rule 1.13(c) requires disclosure outside the corporation only if the action is “clearly a violation of law . . . reasonably certain to result in substantial injury to the organization.” The “tepid approach” to mandatory “whistleblowing” has been debated and retained since its formal adoption by the ABA in 1983.

The final component of the lawyer’s ethical response to client wrongdoing is found in Model Rule 1.2(d). This rule prohibits any lawyer from advising or assisting a client “in conduct that the lawyer knows is criminal or fraudulent.” In the corporate context, Rule 1.2(d) can be viewed as a manifestation of the “public service” type of profession

86 Id. at 55. Furthermore, the actual knowledge standard under Rule 1.13(b) is perhaps even inconsistent with the broad duty under Rule 1.1 to provide competent representation. Id. & n.164. Campell and Gaetke highlight the potential inconsistency:

Model Rule 1.1 states: “A lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for representation.” One might speculate that most cautious lawyers seeking to provide competent representation to their corporate clients would employ a more demanding standard than “actual knowledge” when confronting potentially inappropriate managerial conduct.

87 Cramton et al., supra note 26, at 763.
88 Campbell & Gaetke, supra note 26, at 22.
89 Model Rules of Prof’l Conduct R. 1.13(b) (2009).
90 See Campbell & Gaetke, supra note 26, at 22.
92 Id. R. 1.13(c).
93 Campbell & Gaetke, supra note 26, at 24 (citations omitted).
described by Professor McWilliams that provides cultural support for market transparency where regulations cannot reach. Put differently, "Model Rule 1.2(d) can be viewed as a public interest obligation of lawyers to act to protect society by refusing to assist, and thereby discouraging, their clients' misconduct." In doing so, the Rule provides an "important line beyond which lawyers may not go [when] providing representation to their clients." Rule 1.2(d) works in concert with Rule 1.13 because the lawyer must take reasonable remedial action in the face of client misconduct, the outer limit being withdrawing from representation should the misconduct constitute criminal or fraudulent behavior.

In summary, the Model Rules require actual knowledge of a violation of the securities laws in order for the corporate lawyer to disclose the violation outside of the corporation. In a cultural setting where aggressive corporate management has caused its lawyers to adapt to and essentially become a part of the corporate client's culture, it is not difficult to see the shortcomings of this approach. For a lawyer who feels that his duty is owed primarily to the profit-maximization goals of the firm, and, by extension, to the profit-maximization goals of the firm's clients, the Model Rules do not incentivize the lawyer to perform his gatekeeping function effectively. Further, the standard has been characterized as permissively allowing the corporate lawyer to turn a blind eye to alleged wrongdoing, even when the circumstances call out for further investigation. In a post-Enron world, the approach taken under the Model Rules with respect to the corporate gatekeeper profession is inadequate to ensure investor confidence and good behavior on the part of managers in the securities markets. The "actual knowledge" trigger under Model Rule 1.13(b) has been roundly criticized and enabled behavior that served as the impetus for congressional reform under Sarbanes-Oxley.

III. SARBANES-OXLEY AND SEC REGULATION: STEPS IN THE RIGHT DIRECTION

In contrast to the drafters of the Model Rules, the SEC has explicitly stated its desires to aggressively target corporate transactional lawyers in the post-Enron world. Stephen Cutler, former director of the SEC's Division of Enforcement, explained:

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95 McWilliams, supra note 4, at 259-60.
96 Campbell & Gaetke, supra note 26, at 28.
97 Id. at 29.
99 See supra Part I.
100 Gramton et al., supra note 26, at 755-56.
101 Id. at 755-56; see also Campbell & Gaetke, supra note 26, at 51-57.
102 See Lewis D. Lowenfels et al., Attorneys as Gatekeepers: SEC Actions Against Lawyers in
Consistent with Sarbanes-Oxley's focus on the important role of lawyers as gatekeepers, we have stepped up our scrutiny of the role of lawyers in the corporate frauds we investigate. . . .

A substantial number of SEC enforcement actions in recent years against counsel to public companies (both internal and external) have highlighted the SEC's resolve to hold lawyers liable for not performing adequately their SEC-conceived role as "gatekeepers" to prevent fraud and other securities law violations.103

Mr. Cutler also presented the SEC's rationale: the "themes" of these actions are "the fundamental significance of gatekeepers in maintaining fair and honest markets; . . . the importance of maintaining integrity in the investigative process aimed at ferreting out securities law violations; and . . . the need for greater personal accountability and deterrence at the top of the corporate world."104 SEC officials have gone so far as to cite "extraordinary circumstances" that might require gatekeepers "to report material violations of the law by public issuers [to the SEC]."105 It is clear that corporate attorneys are a primary object of the SEC's attention when it comes to preventing fraud. What remains less clear is the extent to which the Commission will act pursuant to its mandate under Sarbanes-Oxley to disrupt fraudulent behavior while respecting the possible "chilling effect" of "wanting to hold lawyers to an appropriate standard in terms of their roles as gatekeepers."106

A. The Complex Web of Sarbanes-Oxley Regulation

While the rules promulgated under section 307 of Sarbanes-Oxley seem like simple statements of law, buried within those clauses are "numerous complex definitional and interpretive issues."107 In order to understand the practical meanings of the new regime, the phrases "appearing and practicing before the Commission," "in the representation of an issuer," "evidence of a material violation," and "material violation," must be expounded upon.108 "Appearing and practicing before the Commission" is defined as:

(i) Transacting any business with the Commission . . . (ii) Representing the issuer in a Commission . . . proceeding . . . or investigation . . . (iii) Providing
advice in respect of United States securities laws... regarding any document that the attorney has notice will be filed with... the Commission or (iv) Advising an issuer as to whether information... is required... to be filed with... the Commission.\footnote{Id. (quoting 17 C.F.R. § 205.2(a) (2003)).}

A lawyer taking action “in the representation of an issuer,” means “providing legal services as an attorney for an issuer, regardless of whether the attorney is employed or retained by the issuer.”\footnote{Id. (quoting 17 C.F.R. § 205.2(g) (2003)).} A lawyer is defined to have encountered “evidence of a material violation” when she finds “credible evidence, based upon which it would be unreasonable, under the circumstances, for a prudent and competent attorney not to conclude that it is reasonably likely that a material violation has occurred, is ongoing or is about to occur.”\footnote{Id. (quoting 17 C.F.R. § 205.2(e) (2003)).} Finally, “[a] ‘material violation’ is defined as ‘a material violation of an applicable United States federal or state securities law... or a similar material violation of any United States federal or state law.’”\footnote{Id. (quoting 17 C.F.R. § 205.2(i) (2003)).} The plain language of the statute reflects congressional intent that the SEC should have broad regulatory power in the post-Enron era; and the SEC has readily accepted Congress’s mandate.\footnote{See Cutler, supra note 21.}

In contrast to the Model Rules, section 307 of Sarbanes-Oxley instituted an objective culpability predicate that resembles simple negligence. Observers rightly point to Sarbanes-Oxley as an expression of Congress’s desire for the SEC to “change this corporate legal culture and practice and encourage more reporting of dubious corporate activities.”\footnote{Cramton et al., supra note 26, at 752.} Senator Leahy stated the following when introducing a bill predating Sarbanes-Oxley on the floor of the Senate:

This bill can only be part of the needed response to the problems exposed by the Enron debacle. It is clear that changes are needed to restore accountability in our markets... Instead of acting as gatekeepers who detect and deter fraud, it appears that Enron’s... lawyers brought all their skills and knowledge to bear in assisting the fraud to succeed and then in covering it up. We need to reconsider the incentive system that has been set up that encourages... lawyers who come across fraud in their work to remain silent.\footnote{148 Cong. Rec. S1788 (daily ed. Mar. 12, 2002) (statement of Sen. Leahy).}
conclude that it is reasonably likely that a material violation has occurred, is
occurring, or is about to occur.\textsuperscript{116} Through all the verbosity of that sentence
one finds what is essentially a "reasonable person under the circumstances"
standard—simple negligence.

\textbf{B. Isselmann and In re Google: A Lower Threshold in the Post-Enron World}

Despite the relatively clear negligence standard set out by Congress in
Sarbanes-Oxley and the SEC's subsequent interpretation of that mandate,
the vast majority of SEC enforcement actions have consisted of cease-and-
desist proceedings directly implicating the gatekeeper attorney in financial
or accounting fraud because of her failure to provide material information
or for intentionally providing false information to a company's independent
auditors.\textsuperscript{117} Those actions cast little light on what is expected of corporate
lawyers pursuant to the new negligence culpability predicate. Notable
exceptions include SEC v. Isselmann\textsuperscript{118} and In re Google.\textsuperscript{119}

In \textit{SEC v. Isselmann}, the SEC alleged that Isselman, inside general
counsel to ESI, an electronics company, failed "to fulfill his gatekeeper
role [and] was a cause of [the company] reporting materially false financial
results to the public [in violation of] the Commission's rule barring officers
and directors of public companies from omitting to state . . . a material fact
to their accountants."\textsuperscript{120} The charge was based on a scenario in which, as
ESI neared the end of a quarterly reporting period, the company's chief
financial officer ("CFO") and controller sought to fraudulently inflate its
financial results by eliminating vested retirement benefits for its employees
in Asia.\textsuperscript{121}

After this accounting maneuver was executed, $1 million was added
to the company's balance sheet.\textsuperscript{122} Isselmann first heard of this decision
during a meeting of the audit committee in which the CFO assured its
members that the move had been reviewed and approved by ESI's legal
counsel in Japan.\textsuperscript{123} Isselmann's only affirmative act during the meeting

\textsuperscript{116} Cramton et al., \textit{supra} note 26, at 752 (quoting 17 C.F.R. § 205.2(e) (2003) (internal
quotation marks omitted)).

\textsuperscript{117} Lowenfels et al., \textit{supra} note 102, at 879 ("A substantial number of SEC actions
against lawyers post-Sarbanes-Oxley have been cases directly linking the lawyer to financial
or accounting fraud through his or her omitting to furnish material information or providing
false information to a company's independent auditors.").

\textsuperscript{118} Isselmann, Litigation Release No. 18896 (Sept. 24, 2004), 2004 WL 213861, \textit{available
at} http://www.sec.gov/litigation/litreleases/18896.htm [hereinafter \textit{Isselmann}].

\textsuperscript{119} \textit{In re Google}, Inc., Securities Act Release No. 8523 (Jan. 13, 2005), 2005 WL 82435,
\textit{available at} http://www.sec.gov/litigation/admin/33-8523.htm [hereinafter \textit{In re Google}].

\textsuperscript{120} Complaint at 1-2, \textit{SEC v. Isselmann}, No. 04 Civ. 1350 (D. Or. Sept. 21, 2004).

\textsuperscript{121} \textit{Id.} at 2.

\textsuperscript{122} \textit{Id.}

\textsuperscript{123} \textit{Id.} at 3-4.
was to identify ESI's legal counsel in Japan, which caused one member of the audit committee to believe that Isselmann was verifying that counsel's opinion. Soon thereafter, Isselmann consulted with ESI's counsel in Japan and learned that the benefits for ESI's employees in Asia could not be unilaterally eliminated. Isselmann attempted to bring this issue up during a meeting of ESI's Disclosure Committee, but the CFO objected and Isselmann remained silent. After the details of the accounting transaction and the CFO's full involvement in the fraudulent scheme became apparent, Isselmann informed the audit committee. Isselmann's disclosure led to an internal investigation and a restatement of ESI's financial results for the quarter. The SEC instituted a consent proceeding containing its allegations, and Isselmann settled.

Under the guidelines found in the Model Rules, the result in Isselmann is extraordinary. The SEC pursued Isselmann not for affirmative egregious acts but "rather [for] a failure to act under somewhat difficult and ambiguous circumstances requiring in essence an interpretation of Japanese law." The outcome is at least theoretically consistent, however, with the SEC's new enforcement regime promulgated under Sarbanes-Oxley. The SEC's new mandate to enlist a negligence standard in evaluating gatekeeper conduct allows for a practical lesson to be drawn from Isselmann. That lesson, of course, explains the type of behavior the SEC views as negligent. The SEC placed emphasis in its complaint on the fact that Isselmann knew of the faulty legal advice, attempted to alert the audit committee before being rebuffed by the CFO, and refrain from acting as ESI's Form 10-Q was filed with fraudulent financial information. The issue then is whether it was reasonable for Isselmann to let the Form 10-Q be filed fraudulently. The SEC's pursuit of this behavior indicates that a corporate lawyer, faced with a recalcitrant corporate board, must do more than merely voice objection to fraudulent filing or else he is not behaving reasonably. It is unclear from Isselmann's case exactly what constitutes a reasonable course of action.

As in Isselmann, all SEC actions brought under its section 307 authority have been resolved through consent proceedings and thus have not been "tested in the full crucible of an adversarial proceeding." While these

124 Id. at 4.
125 Id.
126 Id. at 5.
127 Id.
128 Id. at 6.
129 See Lowenfels et al., supra note 102, at 887.
130 Id. at 886 (citation omitted).
131 Complaint, supra note 120, at 5.
132 Lowenfels et al., supra note 102, at 887. The SEC is authorized to issue cease-and-desist orders and hold cease-and-desist proceedings pursuant to Section 21C of the Securities Exchange Act of 1934. Such proceedings are often terminated through consent proceedings
cases are ultimately "settled," the simple fact of the charge is enough to devastate a lawyer's professional reputation and irreparably damage his career.\textsuperscript{133} There are serious policy questions that attend such proceedings; most pertinently, how low should the culpability threshold be before the state's regulatory mechanism is triggered, severely damaging an attorney's personal and professional life?

Another example of the SEC acting under Sarbanes-Oxley against a corporate gatekeeper is \textit{In re Google}. In \textit{In re Google}, the SEC brought a cease-and-desist action against Google and David Drummond, Google's inside general counsel, for failure to register over $80 million in securities.\textsuperscript{134} Drummond was tasked with generating legal opinions regarding the applicability of exemptions to cover the entirety of a grant of stock options to employees.\textsuperscript{135} As Drummond learned more about the nature of the stock option plan from the corporate managers, he was forced to search for new and increasingly creative exemptions.\textsuperscript{136} Although concerned with the validity of the exemptions as applied to the stock options, Drummond did not inform the board of directors of his uncertainty when he approved the plan.\textsuperscript{137} When several exemptions failed and the grant of stock options was in violation of securities laws, the SEC began the proceeding against Drummond for failing in his gatekeeper duties.

\textit{In re Google} is another example of the SEC enlisting what appears to be a negligence culpability predicate to allege a violation of a transactional lawyer's gatekeeper duties. Drummond's only culpable act was issuing an incorrect legal opinion regarding the applicable exemptions for the issue of employee stock options. A possible corollary violation would be a failure to monitor Google's corporate managers who continued to issue the options in excess of the maximum covered by the exemptions.\textsuperscript{138} The complaint is unclear as to whether Drummond was informed of the excess at the time, but states that he searched and believed he found other exemptions once he became aware of the excess.\textsuperscript{139} Regardless of whether that constituted a violation of his gatekeeper duties, Drummond was another lawyer snared by the lower culpability predicate in post-Sarbanes-Oxley SEC enforcement.

Both Isselmann and Drummond would have had strong arguments against gatekeeper liability had their cases been tried under a state law

\textsuperscript{133} \textit{Id.} (citation omitted).

\textsuperscript{134} \textit{In re Google, supra} note 119.

\textsuperscript{135} \textit{Id.}

\textsuperscript{136} \textit{Id.}

\textsuperscript{137} \textit{Id.}


\textsuperscript{139} \textit{In re Google, supra} note 119.
that mimics the Model Rules. Each case presents an archetypal situation Congress and the SEC explicitly wanted to prohibit. In Isselmann’s case, so long as he refrained from informing himself by making phone calls to Japan, the CFO could have proceeded and Isselmann would have been shielded from liability due to his lack of knowledge of any violation. As for Drummond, his creative legal opinions regarding the applicable exemptions are the sort of grasping at straws that Congress and the SEC aimed to enjoin by reducing the culpability predicate for gatekeeper liability.

IV. A Two-Tiered System Would More Precisely Calibrate the Regulatory Framework

A. The Current System is Too Broad

The current impasse between aggressive regulation under a negligence standard, as seen in Isselmann and In re Google, and the approach embraced by the Model Rules that absolves all but the most egregious violations can be resolved through a two-tiered approach to gatekeeper liability. The approach to corporate lawyer sanctioning embodied in the Model Rules does not serve as an effective counterweight to the financial and reputational incentives that compel modern corporate lawyers to walk a thin line when it comes to compliance with federal securities laws. The increasingly aggressive client-base that these lawyers serve presents lucrative incentives that the traditional approach does not effectively restrain. The “actual knowledge” standard does not compel the lawyer to “tend the gate” at all. Under this standard, the lawyer has the opportunity to insulate herself from liability by simply walking away from the gate entirely, abdicating her gatekeeping responsibility, and absolving herself from any actual knowledge of who and what passed through.

The series of reforms enacted under the auspices of Sarbanes-Oxley likewise have not provided a satisfactory incentive mechanism; however, these reforms provide a baseline for improvement. In the wake of Enron and several similar scandals, the approach of the Model Rules clearly needed to be supplanted by something in order to combat the paucity of the “actual knowledge” requirement under Model Rule 1.13(b). The broad scope of enforcement granted to regulators coupled with a simple negligence standard has given them necessary latitude to explore and sanction culpable conduct by gatekeeper lawyers. As with many difficult policy issues, however, the regulatory fix comes with a cost. As attorneys

140 See supra Part III.B.
141 See Campbell & Gaetke, supra note 26, at 14 (arguing that the current rules “are too lenient in permitting lawyers to assist managerial wrongdoing”).
142 See supra Part I.
143 See supra Part III.
Isselmann and Drummond discovered, in a post-Enron world, grave consequences might attend arguably non-culpable corporate lawyering.144

In regulating a highly technical and fast-paced legal field, policymakers ought to consider whether the benefit afforded by a simple solution is worth the compliance costs imposed by their regulations. The corporate lawyer’s role as gatekeeper to the securities markets is certainly one that qualifies for close regulatory scrutiny. Her decisions, after all, have implications that emanate through, and thus potentially distort, the efficient functioning of the financial markets. On the other hand, corporate lawyers have a legitimate interest in being free from unwarranted government interference with the execution of their professional duties. In considering a regulatory resolution to serve each competing interest, the current “one size fits all” approach implemented through SEC consent proceedings warrants examination. The broad mandate granted to regulators gives them the power to impose substantial monetary penalties and crippling loss of reputation on attorneys without having to endure the scrutiny of an adversarial proceeding.145

An alternative that would serve both the interests of the regulators in ensuring efficient markets free from manipulation and the interests of corporate lawyers in exercising their professional responsibilities free from undue regulatory constraint lies in a more precise calibration of the level of scrutiny applied to corporate gatekeeper conduct. As currently written, the SEC regulations do not differentiate between negligent and intentional misconduct.146 Yet, the announcement of allegations by the SEC, which is similar for both types of conduct, can subject a corporate lawyer to significant professional hardship.147 The heart of the matter is that the enforcement mechanism currently enabling SEC regulators is too blunt a tool to separate relatively minor infractions from egregious abdications of professional responsibility. In pursuing a policy that would protect American financial markets from the blatant frauds committed by the likes of Enron and its advisors, Congress and the SEC have manufactured a system that punishes well-meaning corporate lawyers executing aggressive but plausible managerial decisions similarly to those who willfully defraud the market community. While there is no counterfactual information available to support a claim that the current policy has chilled innovative corporate activity, the respective plights of Isselmann and Drummond148 should at least give pause to supporters of the present scheme.

144 See supra Part III.B.
145 See Lowenfels et al., supra note 102, at 887.
146 See supra Part III.A.
147 See Lowenfels et al., supra note 102, at 887 (Many SEC actions are “terminated through consents incorporating only the SEC’s allegations” because “the lawyer’s reputation and livelihood have already been destroyed by the charges alone.”).
148 See supra Part III.
B. The Two-Tiered Approach

A two-tiered approach that more precisely targets the type of culpable behavior would be superior to the current enforcement mechanism. Such a system would differentiate between reckless or intentional misconduct on the part of corporate gatekeepers and misconduct which is merely negligent. As it is currently constituted, the enforcement regime consists largely of cease-and-desist proceedings that are terminated through consent agreements. Because proceedings targeting egregious conduct garner disproportionate attention but are classified the same as proceedings premised on less culpable conduct, those lawyers subject to discipline for minor infractions find themselves disproportionately punished.

To be sure, SEC enforcement efforts serve a vital role in protecting the integrity of the market system. Those efforts, however, must be carefully balanced to avoid upsetting the efficiency of the system they seek to protect. A more carefully calibrated system that formally recognizes the distinction between intentionally or recklessly fraudulent behavior on the one hand, and merely negligent behavior on the other, would better serve the SEC's mandate and the markets it seeks to protect.

C. The Spiegel Case

The benefits of the proposed framework are aptly demonstrated by comparing the enforcement actions described above with the SEC's case against Spiegel, Inc. In 2003, the SEC filed a civil complaint against Spiegel, alleging fraudulent non-disclosure of financial information on a Form 12b-25 filed with the Commission. The facts of the Spiegel case present a paradigmatic example of the kind of situation the current SEC approach was designed to address. In that respect, the Spiegel case serves as a counterweight to the cases initiated against Isselmann and Drummond. By focusing specifically on the lawyers and their respective roles in corporate behavior, the vastly different situation described below provides compelling support for bifurcating the current SEC enforcement procedure.

Spiegel, the mail order retailer and former operator of the Eddie Bauer clothing chain, was a Delaware corporation controlled by German

149 See sources cited supra note 138.
152 Id. at *27-28.
businessman Michael Otto, who owned a ninety percent equity stake. In 1999, the corporation instituted an “easy credit” program, extending credit to unqualified purchasers and selling the receivables to various special purpose vehicles through an asset backed securitization program. When the economy slowed, many of the credit program’s customers defaulted, causing Spiegel to default on several loan covenants and bringing the company to the brink of bankruptcy. Efforts to reorganize the agreements and improve its general financial situation failed, causing Spiegel’s independent auditors to inform the company that it would issue a “going concern” opinion, alerting interested parties that the auditors doubted its ability to continue doing business.

The situation described above summarizes the facts as Spiegel’s outside lawyers, from the firm Kirkland and Ellis, understood them at the time Spiegel’s Form 10-K annual report for the year 2001 came due. Those lawyers advised Spiegel to file the Form 10-K in late May 2002. Mr. Otto and the rest of the Spiegel executive and audit boards, however, declined to file the 10-K, fearing it would alert investors and creditors to the “going concern” opinion. Instead, Kirkland and Ellis lawyers filed several Forms 12b-25 in lieu of the Form 10-K and subsequently unfiled Forms 10-Q. These records were filed despite the lawyers’ full knowledge that they fraudulently misstated the truth behind the nondisclosures. There is no record of the lawyers from Kirkland and Ellis advising Spiegel of the perils of its failure to file the forms and thus make non-fraudulent disclosures to its shareholders. Spiegel eventually filed a Chapter 11 bankruptcy petition. Despite reprimands contained in the Independent Examiner’s Report accompanying the final order, there appears to be no public record of a settlement between Kirkland and Ellis and the SEC.

153 See Lowenfels et al., supra note 102, at 892 (citation omitted).
155 Id. at *2-3.
156 Id. at *3.
157 Id.
158 Id. at *28.
159 Lowenfels et al., supra note 102, at 895.
160 Id. at *104.
161 Id. at *45-46.
162 Id. at *45-46.
163 Kirkland and Ellis maintains that the Forms 12b-25 that it filed on behalf of Spiegel were not incorrect. See id. at *27 n.14. The firm also maintains that Forms 12b-25 are not themselves disclosure documents, and therefore, no breach of the SEC’s disclosure requirements occurred. Id. The Independent Examiner’s Report, however, states that “[t]here does not appear to be a record” of Kirkland and Ellis advising Spiegel “of the dire consequences of
may be a simple explanation for this, however, as the Kirkland and Ellis lawyers were not subject to the higher standard of Sarbanes-Oxley because their conduct occurred before its enactment.\textsuperscript{165}

A comparison of the facts underlying the Spiegel case with those underlying Isselmann's and Drummond's cases demonstrates the value of the two-tiered approach: it would permit the SEC to sanction truly culpable behavior while sparing those lawyers whose negligence does not warrant severe punishment.

Neither Drummond nor Isselmann acted entirely appropriately. Each party made missteps, however, they did so in a dynamic environment and, at worst, with a negligent state of mind. The lawyers in the Spiegel case, meanwhile, actually knew the filings were fraudulent and went ahead, facilitating the fraudulent behavior. Although there is no record of sanctions against the Spiegel lawyers,\textsuperscript{166} their behavior is more culpable because they had actual knowledge of the fraud. A two-tiered system would distinguish these types of situations, giving SEC regulators latitude in the types of orders it seeks to impose on gatekeeper attorneys, sensitive to the harsh results of the instigation of any SEC investigation into a corporate lawyer's practice.

In order to accomplish results consistent with the two-tiered system, the SEC would need a mechanism whereby it could bifurcate its charging orders in order to distinguish between different culpability predicates. The current cease-and-desist order would suffice to continue as the charging mechanism for reckless or intentional violations. The key innovation of the two-tiered system would be to invent a new and separate charging mechanism for those lawyers whose conduct was merely negligent. The structure and form of the order might be similar to that of the cease-and-desist order, but the connotations of impropriety would be reduced, thereby subjecting less culpable lawyers to less onerous treatment. Further, in order to prevent the machinations of some who might abuse the two-tiered system by routinely acting negligently, some mechanism could be installed whereby persistent negligent offenders would graduate to the harsher treatment of the cease-and-desist order. Of course, there is no silver bullet to prevent corporate fraud in the realm of securities law. The two-tiered approach, however, merits consideration for the more precise calibration it gives to the regulatory efforts of the SEC.

\textsuperscript{165} Id. at *44.

\textsuperscript{166} See supra note 164 and accompanying text.
V. CONCLUSION: THE LOGIC OF THE TWO-TIERED APPROACH

The premise underlying the two-tiered approach is that different levels of corporate gatekeeper liability ought to be treated differently by SEC regulators. A two-tiered approach to SEC regulation of the corporate gatekeeper professions would be vastly superior to the current one-size-fits-all approach. Under such a system, lawyers who in good faith complied with their duties, but were simply negligent, would be subject to a different enforcement process than those who willfully violated securities laws on behalf of their clients. The current system has the potential to ruin a lawyer's professional career for a single mistake made in a complex and fast-paced environment. A two-tiered system would avoid such results. The primary benefit of a two-tiered system is that it serves each policy that a good SEC regulation should: it protects passive investors from manipulation of the securities markets by corporate insiders while protecting those corporate insiders from obtrusive oversight that would interfere with their primary duties to maximize shareholder profit. In this way, the transactional attorney will be in a better position to effectuate what has long been her stated role: that of the corporate gatekeeper.