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THE 2003 BOTEIN AWARDS WERE PRESENTED AT THE ASSOCIATION ON March 31, 2003. The Awards, dedicated to the memory of Bernard Botein, former President of the Association and Presiding Justice of the First Department, have been presented annually since 1976 to pay tribute to court personnel in the First Department who have made an outstanding contribution to the administration of the courts.

This year’s recipients are: Joseph Bleshman, Esq., Deputy Clerk, Appellate Division, First Department; Steven B. Clark, Court Clerk Specialist, Bronx Supreme Court, Criminal Division; Jacqueline Dupree, Citywide Manager of Data Entry Operations, Criminal Court of the City of New York; Esther E. Kelly, Case Management Coordinator, Supreme Court, Bronx County; Paul Moriarty, Esq., Deputy Chief Court Clerk, Bronx County Family Court; and Evelyn C. Spence, Principal Administrative Services Clerk, Supreme Court, Civil Branch.

The Awards are made possible by a grant from the Ruth and Seymour Klein Foundation, Inc.

ON FEBRUARY 24, THE ASSOCIATION PRESENTED THE KATHRYN A. McDonald Award for excellence in service to the Family Court to Kay Crawford Murray and Harriet R. Weinberger. Both have demonstrated the commitment to children and the energy and dedication to the work of the Family Court that merit their receiving this award. The award is named for the long-time Administrative Judge of the New York City Family Court.

WAYNE STATE UNIVERSITY SCHOOL OF LAW WAS NAMED THE WINNER of the Final Rounds of the 53rd Annual National Moot Court Competition held at the Association on January 27-30. The competition is co-
THE FOLLOWING NEW COMMITTEE CHAIRS HAVE RECENTLY BEEN appointed. Beatrice S. Frank (Task Force on Women in the Courts); Christopher McKenzie (International Environmental Law); Andrea S. Rattner (Employee Benefits); Elaine S. Reiss (Administrative Law); Bryan C. Skarlatos (Personal Income Taxation); and Phil Weinberg (Downtown Redevelopment).
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Copies of any of the above reports are available to members by calling (212) 382-6624, or by e-mail, at khuggins@abcny.org.
Antitrust “Market Power” and Intellectual Property: Why FTC and DOJ Action is Necessary

The Committee on Antitrust and Trade Regulation

INTRODUCTION

In 1989 and again in 1995, the Judiciary Committee of the House of Representatives considered legislation that would have prohibited courts in antitrust cases from drawing a presumption of a relevant market, or of the existence of market power, based merely on the possession of a patent or copyright. In both instances, the Department of Justice endorsed the substance of the proposed legislation but questioned whether a substantial and compelling justification for amending the antitrust laws existed. In 1996, when Assistant Attorney General Joel Klein testified on behalf of the Antitrust Division before the Committee, he described the Ninth Cir-


cuit opinion in Digidyne Corp. v. Data General Corp. as the “lone decision” since the Supreme Court's dicta in Jefferson Parish Hospital District No. 2 v. Hyde to presume market power from the existence of intellectual property. Mr. Klein, citing several post-Digidyne cases in which the use of such a presumption was rejected, concluded that the “inexorable development and maturation of court decisions in this area” was one reason why legislative action was unnecessary.

Since the time of Mr. Klein's testimony, the case law in this area has not matured in the direction he thought it would. To the contrary, despite virtually unquestioned economic logic undermining the use of the presumption, some courts, in decisions we examine below, continue to apply it. Thus, the House judiciary Committee once again considered a legislative correction to the problem. On behalf of the Association of the Bar of the City of New York, we urge the FTC and DOJ (the “Agencies”) to seek to clarify the law in two respects. First, the Agencies should participate as amici in any petition for certiorari to the Supreme Court addressing the presumption that market power arises from intellectual property. Second, in the event the House or Senate considers an overall package of intellectual property legislation, the Agencies should support legislation as part of such a package that states that a patent, copyright, or trademark does not alone support a presumption that its holder possesses market power or that the intellectual property constitutes its own relevant market.

THE PRESUMPTION MAKES NO ECONOMIC SENSE

The antitrust laws and the patent laws are complementary in that both seek to promote “innovation, industry and competition.” Continued judicial reliance on a presumption that the mere existence of intellectual property confers market power, however, risks undermining this harmony. As Professor Hovenkamp has put it, “presum[ing] market power in a product simply because it is protected by intellectual property is nonsense.”

3. 734 F.2d 1336 (9th Cir. 1984).
The mere grant of a patent or copyright does not create demand for a particular product, nor shield it from competition. It tells us nothing about the presence or absence of substitutable products, the nature or extent of barriers to entry, or the ability of its owners to profitably raise price or reduce output. That is to say, the mere existence of intellectual property tells us nothing about whether market power exists. In Professor Areeda's words, "[e]xcluding others from using a particular name, word, image, product, or process does not imply any substantial market power when substitutes are plentiful. Trademark, copyright, or patent excludes others from duplicating the covered name, word, or product (etc.) but does not typically exclude rivals from the market. Accordingly, market power cannot be inferred, even presumptively, from the possession of intellectual property."

There is certainly nothing inherent in the nature of intellectual property that justifies a difference in treatment under the antitrust laws from any other type of product. While it might as a general proposition be true that intellectual property is characterized by high fixed costs and extremely low marginal costs, thus rendering traditional marginal cost pricing insufficient to recoup the sunk R&D investments, pricing above marginal cost does not imply the existence of market power. It does not make the question of whether substitutes or entry barriers exist irrelevant. Competition and new (or potential) entry in markets in which a patented technology is deployed will still constrain the exercise of market power. Rather, it is the inherent nature of intellectual property that makes use of the presumption so potentially harmful to incentives to innovate—it is relatively easy to obtain and, as former Chairman Pitofsky has noted, "[o]n average, market power probably is less durable in the high-tech sector of the economy."  

Simply put, continued judicial use of the presumption defies common sense and risks harming the very competitive process the antitrust laws are designed to protect. The implicit justification for using the presumption—that, like per se categories of unlawfulness, it creates a rule that is simple, comprehensible, and easy to administer—fails to withstand

scrutiny. Economic theory has done much to limit the range of conduct subject to per se condemnation, and similarly has much to offer in demonstrating that a presumption of market power based simply on ownership of intellectual property risks condemning conduct that may be welfare-enhancing and procompetitive.

THE ANTITRUST AGENCIES' GUIDELINES

Noting that the law is "unclear," the Agencies' Antitrust Guidelines for the Licensing of Intellectual Property (1995)\(^\text{11}\) nonetheless state that the Agencies "will not presume that a patent, copyright, or trade secret necessarily confers market power upon its owner. Although the intellectual property right confers the power to exclude with respect to the specific product, process, or work in question, there will often be sufficient actual or potential close substitutes for such product, process, or work to prevent the exercise of market power."\(^\text{12}\) This guiding principle of Agency enforcement policy is a direct corollary of the fundamental proposition underlying the Guidelines—that intellectual property should be treated no differently from any other form of property.

The Guidelines, however, are not binding on the courts, do not preclude private litigation, and do not obviate the need to clarify the law. That there is an inconsistency between Agency enforcement policy and the position taken by some courts further confuses the state of the law. Judicial use of the presumption is economically irrational and risks creating, rather than remedying, a market failure by undermining the incentives to invest that the patent laws strive to promote. The Guidelines stand out starkly as further evidence of the need for Supreme Court clarification or, in the event that the House or Senate considers overall changes in the intellectual property statutes, legislative clarification.

THE JURISPRUDENCE

The question of intellectual property and market power arises most frequently in tying cases, where the existence of market power is nearly outcome-determinative to a finding of antitrust violation. Unlawful tying occurs where the seller conditions the sale or license of one product


\(^{12}\) Id. at § 2.2 and n.1.
(the tying product) on the sale or license of another (the tied product). The Supreme Court, in United States v. Loew's, Inc., stated that the "economic power" required for a tying violation is "presumed when the tying product is patented and copyrighted."\(^{13}\) In many tying cases since, the Supreme Court has stated that the existence of a patent or copyright on the tying product creates a presumption of market power, and the Court has never suggested any retreat from this principle.\(^ {14}\) In its most recent decision addressing this subject, Jefferson Parish, the Court in dictum gave new life to the controversy by stating that "if the government has granted the seller a patent or similar monopoly over a product, it is fair to presume that the inability to buy the product elsewhere gives the seller market power."\(^ {15}\) Justice O'Conner, for the minority in a 5-4 concurrence, criticized the presumption by stating that "a patent holder has no market power in any relevant sense if there are close substitutes for the patented product."\(^ {16}\)

The use of intellectual property as a proxy for market power is particularly troublesome in the tying context given the currently confused state of tying law itself. Tying doctrine today is governed largely by the Supreme Court's decision in Jefferson Parish. That Court established as a threshold element to an unlawful tying arrangement a showing that there is significant market power in the tying product, such that the power is of "the degree or the kind" that enables the seller of the tying product to "force" customers to purchase the tied product.\(^ {17}\) If such market power exists, then under Jefferson Parish the tying can be declared unlawful per se and no inquiry into the possible procompetitive benefits or efficiency justifications for the tie-in will be considered.\(^ {18}\) The Court of Appeals ruling in United States v. Microsoft Corp.\(^ {19}\) contributed substantially to the

\(^{13}\) 371 U.S. 38, 44 (1962).


\(^{15}\) Jefferson Parish, 466 U.S. at 16, citing Loew's and Paramount Pictures.

\(^{16}\) Id. at 38 n.7

\(^{17}\) Id. at 17-18.

\(^{18}\) In addition to a showing of market power, the other necessary elements of the per se offense must be met: the tying and tied product must in fact be separate products, and a "not insubstantial" amount of commerce must be affected. See, e.g., Fortner I, 394 U.S. at 498-99.

\(^{19}\) 253 F.3d 34 (D.C. Cir. 2001) (en banc).
erosion of this per se rule by attempting to carve out what might be called a “technology exception” to that rule. Reasoning that in the “pervasively innovative” platform software industry, traditional per se analysis risks condemning ties that may be welfare enhancing and procompetitive, the D.C. Circuit declined to apply the per se rule to strike down Microsoft’s “bundling” of Internet Explorer (the tied product) with the Windows operating system (the tying product).\textsuperscript{20}

The Microsoft ruling, though arguably inconsistent with Jefferson Parish, does accord with the tying analysis in the Guidelines, which reject per se treatment of tying even in the face of evidence of market power. Tying is likely to be challenged by the Agencies where “(1) the seller has market power in the tying product; (2) the arrangement has an adverse effect on competition in the relevant market for the tied product; and (3) efficiency justifications for the arrangement do not outweigh the anticompetitive effects.”\textsuperscript{21}

In weighing the risks of investment in R&D against the strength of protection for the resulting invention, companies currently have the following guidance: The Supreme Court has said that if the tying product is protected by patent or copyright the existence of market power should be presumed. At least two federal appellate courts agree.\textsuperscript{22} The Agencies and some lower and appellate courts disagree, and treat intellectual property no differently from other property. The Supreme Court has said that, where all the elements of a tying claim have been met, it should be struck down as per se illegal without a balancing of any potential efficiency gains against harm to competition. The Agencies and some lower courts disagree, arguing that a rule of reason market analysis to measure net efficiencies is indispensable to achieving the welfare-maximizing outcome, particularly in hi-tech industries.

Such uncertainty leaves the law in this economically significant area in a state of turmoil and unreliability. Post-Jefferson Parish lower court jurisprudence provides little comfort. In Digidyne, the Ninth Circuit held that a copyright in an operating system was sufficient to trigger a presumption of market power in that product market, thus rendering the linking of sales of that operating system to sales of central processing units per se unlawful tying. Rather than analyzing whether customers, in

\textsuperscript{20} Microsoft, 253 F.3d at 93.
\textsuperscript{21} GUIDELINES, \textsuperscript{22} Digidyne; MCA Television Limited v. Public Interest Corporation, 171 F.3d 1265 (11th Cir. 1999).
this instance OEMs, had alternatives to the tying product, the Court expressly refused to review the record for “what it may reveal as to defendant’s position in a defined market,” and instead focussed only on considering whether the tying product was “sufficiently unique and desirable to an appreciable number of buyers....” Citing Loew’s for the proposition that a copyright establishes such uniqueness as a matter of law, the Court concluded that the copyright “created a presumption of economic power sufficient to render the tying arrangement illegal per se.” Not only did this analysis deem demand-side substitutability to be irrelevant in the face of a copyright, but, even if it existed, incapable of diminishing the “adverse impact on competition in the tied product.”

Nor has judicial use of the presumption been confined to tying. In Image Technical Services, Inc. v. Eastman Kodak Co., the Ninth Circuit concluded that, when a seller has market power, a mere refusal to license a patented product to a competitor can violate Section 2 of the Sherman Act as an act of monopolization. The liability finding was based on the patent owner’s subjective intent and the assumption of market power for the patented product—introducing enormous uncertainty into whether an IP owner has the right to refuse to license intellectual property. This analysis was rejected in In re Independent Service Organizations Antitrust Litigation, where the Federal Circuit agreed that “[a] patent alone does not demonstrate market power.” In fact, many appellate courts have recog-

23. Digidyne, 734 F.2d at 1341.
24. Id. at 1344.
25. Id. at 1345.
26. 125 F.3d 1195 (9th Cir. 1997).
28. Id. at 1325. Former FTC Chairman Pitofsky has criticized this ruling for other reasons, noting that “because intellectual property is now a principal, if not the principal, barrier to new entry in high-tech markets, ... I am concerned that recent cases, and particularly the Federal Circuit’s opinion in [In re Independent Service Organizations Antitrust Litigation] have upset the traditional balance between intellectual property and antitrust in a way that has disturbing implications for the future of antitrust in high-technology industries.” 68 Antitrust L.J. 913, 919 (2001). Chairman Pitofsky referred to a danger that the market power that may result from intellectual property protection could be “used to distort competition in, for example, related product or service areas.”
nized that a presumption of market power is economically unsupportable in Section 2 cases, and have declined to follow the Jefferson Parish dictum. No economic theory has been advanced to suggest why application of the presumption might be more appropriate in tying cases.

Nor does the Supreme Court seem inclined to resolve the inconsistency. In two pre-Digidyne cases, the Supreme Court twice denied certiorari in cases presenting the question of whether market power should be presumed from the existence of intellectual property. In its most recent opportunity to confront the issue, it also declined to hear Digidyne, though Justices Blackmun and White dissented, urging the Court to address the issue of “what effect should be given the existence of a copyright or other legal monopoly in determining market power.” The Court denied certiorari notwithstanding clearly divergent lower court jurisprudence, but also in the face of inconsistency with the Supreme Court’s own prior decisions. In Walker Process, the question before the Court was whether enforcement of a patent obtained by fraud could be the basis of a Section 2 monopolization claim. Expressing a reluctance to find per se illegality “absent examination of market effect and economic consequences,” the Court held that even in the face of a fraudulently procured patent, all the elements of a Section 2 claim must be established, including market power. “There may be effective substitutes for the device which do not infringe the patent. This is a matter of proof....” Yet this case was decided after Loew’s, where that very factual analysis was deemed unnecessary in a tying case.

As a matter of antitrust policy and sound economics, Digidyne was wrongly decided. Most disturbing, however, is that as a strict matter of law the outcome was correct. It was consistent with established Supreme

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31. 473 U.S. at 909.


33. Id
Court precedent both in use of the presumption of market power and in application of the per se rule against tying. As the Supreme Court has said on several occasions, lower courts—even a court of appeals sitting en banc—lack the power to overrule prior Supreme Court decisions.34

DÉJÀ VU ALL OVER AGAIN

In Assistant Attorney General Klein’s 1996 testimony to the House Judiciary Committee, he questioned the need for legislation in light of the “inexorable development and maturation of court decisions,” but supported its substance.35 To illustrate the baselessness of the presumption, Mr. Klein used the following example:

[A]s the Court mused in a footnote in Loew’s, the film distributors’ ability to foist undesirable films on unwilling television stations may have stemmed from ‘the fact that to television as well as motion picture viewers there is but one Gone With the Wind.’ Had the Court relied on that point, Loew’s would be a far more compelling—but much narrower—case, in which the market power finding was premised on the actual attributes of a tying product. Instead, though, the Court presumed market power from the very existence of the copyright, which vested no more power in Gone With the Wind than it did in Getting Gertie’s Garter, one of the tied movies. But if that were what mattered, the movie studios would not have needed to tie in the first place—market power would exist for every copyrighted movie. This is one of the clearest examples of why it is wrong to infer market power from the mere existence of an intellectual property right.36

Yet, in MCA Television Limited v. Public Interest Corporation,37 decided three years after Mr. Klein’s testimony and in precisely the same “block booking” context, the Eleventh Circuit employed the presumption. MCA licensed several syndicated television shows to PIC, and conditioned these licenses on agreement by PIC that it would also license a show called Harry and the Hendersons. PIC later alleged that it would not have licensed

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36. Id. at *2 (citations omitted) (emphasis added).
37. 171 F.3d 1265, 1277 (1999).
Harry had MCA not insisted on this contractual provision. The Eleventh Circuit, without so much as a footnote devoted to the uncertainty in the case law regarding a presumption of market power, simply applied Loew's and presumed that MCA's copyright in the tying television shows conferred upon it economic leverage sufficient to induce PIC to take the tied product (Harry). The court concluded:

Conditioning the licensing of the shows PIC did wish to license on its cash purchase of Harry thus allowed Harry to best the competition for the slot it eventually filled on PIC's roster entirely apart from its intrinsic appeal to PIC's programmers. This is precisely the sort of anticompetitive effect the per se rule of Paramount and Loew's intended to protect against, and unless and until the Supreme Court explicitly overrules these cases, we must adhere to the rule that they establish.38

The Court does not even mention by name what the tying products are, let alone conduct any sort of analysis to determine whether these shows were sufficiently popular to actually give to MCA the ability to charge supracompetitive prices, and thereby “force” PIC to also license Harry. Demand for programming turns not on whether it is copyrighted, but on whether it is desirable. Similarly, desirability has nothing to do with the presence or absence of a copyright. To borrow Assistant Attorney General Klein’s words, “[t]his is one of the clearest examples of why it is wrong to infer market power from the mere existence of an intellectual property right.”39

THE PATENT LAWS DO NOT PROVIDE THE SOLUTION

Given recent history, the Agencies must urge the Supreme Court to take the first opportunity to correct the Jefferson Parish dictum. Moreover, if overall intellectual property legislative reform is under consideration, then a provision to cure this particular inconsistency appears appropriate. The patent laws have been repeatedly amended over the years to provide greater protection to intellectual property. Most recently, for example, Section 271(d) of title 35 was amended in 1988 to provide:

No patent owner otherwise of a patent entitled to relief for

38. Id. at 1278 (citations omitted).
infringement or contributory infringement of a patent shall be denied relief or deemed guilty of misuse or illegal extension of the patent right by reason of his having done one or more of the following...5) conditioned the license of any rights to the patent or the sale of the patented product on the acquisition of a license to rights in another patent or purchase of a separate product, unless, in view of the circumstances, the patent owner has market power in the relevant market for the patent or patented product on which the license or sale is conditioned.

Though the economic logic of this amendment is unquestionable, some courts have taken the position that Section 271(d) applies only to patent misuse defenses in infringement cases, not antitrust cases. The Agencies have apparently taken a similar position—Section 271(d) is not mentioned in the Guidelines.

CONCLUSION

In his 1996 testimony before the Committee, Assistant Attorney General Klein stated, we think correctly, that “modification of the application of the antitrust laws should occur only when there is a substantial and compelling justification in favor of the change.” That justification exists today. The case law is confused and the patent laws do not solve the problem. Adherence to governing Supreme Court precedent compels application of the presumption in tying cases—a result inimical to the aims of both the patent laws and the antitrust laws.

The incentives that the patent laws provide to foster innovation may well be undermined if the innovator can be saddled with a presumption of market power—the presumption increases the risk of litigation being filed, the threat of treble damages and of ultimate liability, and so correspondingly reduces the value of intellectual property. “The benefits from innovation are generally not fully recovered by the inventor, particularly

40. Grid Sys. Corp. v. Texas Instrs., Inc. 771 F. Supp. 1033, 1044 n.2 (N.D. Col. 1991) (“Section 271(d) relates only to the defense of patent misuse as a defense to an infringement claim.”); accord, e.g., ITS v. Kodak, 125 F.3d 1195, 1241 n.7 (9th Cir. 1996). Other courts, however, have held that this section does apply in antitrust cases. See, e.g., Polysis v. Fuller, 709 F. Supp. 560, 576 (E.D. Pa.) (Under 271(d), absent market power, a party "cannot be guilty of either antitrust violations or patent misuse..."); aff’d mem., 889 F.2d 1100 (Fed. Cir. 1989); see also Intergraph Corp. v. Intel Corp., 195 F.3d 1347, 1362-63 (Fed. Cir. 1999); Data Gen. Corp. v. Grumman Sys. Support Corp., 36 F.3d 1147, 1187 (1st Cir. 1994).

where the legal regime for protecting the invention is weak. Antitrust rules which reduce the value of intellectual property or discourage broad exploitation of intellectual property may therefore impose a more substantial social cost than similar rules applied to other forms of property.”42

The Agencies should encourage the Supreme Court, through amici submission in support of petitions for certiorari and on the merits of the issues presented, to correct the Jefferson Parish dictum that market power should be presumed from a “patent or similar monopoly over a product.” Alternatively, in the event the House or Senate considers overall intellectual property reform, the Agencies should support legislation as part of that package that a patent, copyright, or trademark does not alone support a presumption that its holder possesses market power or that the intellectual property constitutes its own relevant market.43

December 2002


The Committee on Antitrust and Trade Regulation

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The Committee approved this document by an affirmative vote of 33 members. Two members abstained from voting and one member dissented. Adjunct members of the Committee are not invited to vote on Committee documents. The Committee wishes to thank the primary authors of this paper, Abid Qureshi and John Herfort, for their efforts.
Comments on Rules Implementing Section 307 of the Sarbanes-Oxley Act: Standards of Professional Conduct for Attorneys Practicing Before the SEC

These comments were filed by the Association of the Bar on December 16, 2002, in response to draft rules proposed by the Securities and Exchange Commission. The comments reflect the work of representatives of five Association committees, all of whom are listed at the conclusion of the report.

PRELIMINARY STATEMENT

In response to a series of recent disclosures of corporate misconduct and with the goal of restoring investor confidence, Congress enacted the Sarbanes-Oxley Act of 2002 (the “Act”). Section 307 of the Act required the Securities and Exchange Commission to establish rules within 180 days which would set forth minimum standards of professional conduct for attorneys appearing and practicing before the Commission in the representation of issuers of securities. The rules were to require an attorney to report evidence of material violations of securities law or breaches of fiduciary duty by the company or its agents to the chief legal counsel or officer
(“CLO”) or chief executive officer (“CEO”). If this failed to produce an appropriate response, then the attorney would be required to “go up-the-ladder” within the company by reporting the problem to an audit committee, an independent set of directors or, if necessary, the full board of directors.

The Association of the Bar for the City of New York (“CityBar”) fully supports Section 307 of the Act. The legislation is consistent with ethical prescriptions contained within New York’s Code of Professional Responsibility (“New York Code”) and the American Bar Association’s Model Rules of Professional Conduct (“Model Rules”).1 In defining the obligations of an attorney representing an organization, including an “issuer” of securities, both the New York Code and the Model Rules begin with recognition that the lawyer’s client is the organization, not its constituents—officers, employees, directors or individual shareholders. (22 NYCRR §1200.28; Model Rules 1.13). As well, we endorse the proposition that “[t]he lawyer is part of a judicial system charged with upholding the law. One of the lawyer’s functions is to advise clients so that they avoid any violation of the law in the proper exercise of their rights.” (Comment, Model Rules 1.6). Accordingly, in order for the attorney to act “in the best interest of the organization,” both the Code and the Model Rules require the attorney to report violations of law by officers, employees or agents of the company up-the-ladder when the violations “might be imputed to the company” or otherwise are “likely to result in substantial injury to the company.” Id. For that reason, we welcome the Act and support proposed rules consistent with the Act.

Unfortunately, the Commission, in its first draft, has proposed rules that we believe go beyond, if not counter to, the Act’s language and intent. The rules impose obligations requiring or, in some circumstances, allowing an attorney to act against the client’s interest and over its objection, including: (1) withdrawal from representation; (2) public notification to the Commission of withdrawal; (3) affirmative disavowal of documents filed on the client’s behalf with the Commission; (4) creation and maintenance of non-privileged documentation by the attorney of wrongdoing within the organization which may then be used against the organization; (5) disclosure of confidential client information; and (6) disclosure of privileged information. The net practical effect of the proposed rules would be to require an attorney, concerned about personal liability, to investigate and report actions and statements of employees either working

1. There are some differences in approach between the New York Code, the Model Rules and the Act regarding “up-the-ladder” reporting—some of which are discussed within this report—but in practice there is more coincidence than conflict.
for an issuer or associated with an issuer and then, if not satisfied with the response, to report misconduct to the SEC. The rules as drafted, if aggressively enforced, could eviscerate the attorney’s traditional role as advocate, confidant and advisor. This would drive a wedge between attorney and client. Corporate officers and employees would not be forthcoming and this, in and of itself, would in the long run hurt the corporation and its investors. As explained in the report that follows, the rules ask an attorney to give a higher priority to documentation and reports to the SEC than to the interests of the corporation. As well, an attorney fearing disciplinary sanction, civil liability or potential criminal exposure for a failure to report misconduct by others is asked to document and expose client confidences over the client’s (the corporation’s) objection when disclosure might well not be in the client’s interest. If the rules are created to protect the client corporation from malfeasance by wayward employees or agents, the client-corporation, through, for example, a board of directors exercising proper business judgment, should have a voice in deciding whether attorney-client secrets or confidences will be disclosed.

It is not possible to explore in adequate depth the many issues and problems raised by the proposed rules in the brief time, thirty days, that we have been allotted to prepare comments upon the proposal. (The Act was signed into law in July but only specified “up-the-ladder” reporting. Rules requiring withdrawal, documentation, disclosure and disaffirmance were added by the Commission in its November release.) However, we have endeavored to highlight a few issues of significance in this report. As well, since we continue to support the stated objectives of the Act, we offer suggestions for implementing regulations that we believe are consistent with our recognized obligation to contribute to confidence in the securities market by requiring a high standard of professional conduct from attorneys who practice before the Commission.

At the outset, it should be noted that we share many points of agreement with the proposed rules and find support for them in the New York Code, Model Rules and existing decisional law. Our greatest concern is with the disruption to the attorney-client relationship and with those provisions that hold an attorney accountable for frauds or omissions performed by others, without the lawyer’s assistance or participation, and where the attorney may not have actual knowledge of the wrongdoing.

Points of Agreement
A legitimate, and we believe persuasive, argument can be made that the Act granted only a limited rule-making authority to the Commission.
Up-the-ladder reporting is mandated, but the proposed rules requiring withdrawal, record-keeping, disaffirmance, and disclosure go beyond statutory authority. As well, we argue later, that those issues, as a matter of policy, history and law, are best left with Congress, the States and Bar Associations. However, before highlighting our differences with the Rules, it’s necessary to place those differences in context by explaining essential points of confluence with the Commission’s proposal. The Model Rules and the New York Code, along with opinions further explaining them by the pertinent Bar Committees, have provisions which address these same issues. They provide a framework which can and should provide the Commission with an abundance of authority to demand honesty, competence and professional behavior from lawyers who practice before it.

- The Commission has the right to, and should, censure or bar an attorney from practicing or appearing before it when the attorney has engaged in misconduct in the representation of an issuer. The New York Code defines prohibited misconduct to include “dishonesty, fraud, deceit, or misrepresentation.” DR 1-102 (A)(4). That provision should be incorporated within the Commission’s rules.

- The Commission has the right to demand, consistent with Model Rules 4.1 (“Truthfulness in Statements to Others”), that an attorney not knowingly make a false statement of material fact or law to the Commission, or fail to disclose a non-confidential material fact when necessary to avoid assisting a criminal or fraudulent act by the client.

- Further, we agree that the Commission should expect compliance with the New York Code that a lawyer shall not counsel or assist the client in conduct that the lawyer knows to be illegal or fraudulent; knowingly make a false statement of law or fact; or knowingly fail to disclose that which the lawyer is required by law to reveal. (See, generally, DR 7-102, “Representing a Client Within the Bounds of the Law”).

- We support a rule that a lawyer may reveal, over the objection of the client, the intention of a client to commit a crime and confidential or secret information necessary to prevent the crime. (DR 4-101(C)(3)).

- As well, we support the rule that confidences or secrets may be revealed, over the client’s objection, to the extent implicit in disaffirming a written or oral opinion or representation previously given by the lawyer and believed by the lawyer still to be
relied upon by a third person where the lawyer has discovered that the opinion or representation was based on materially inaccurate information or is being used to further a crime or fraud. (DR 4-101[C][5].)

• With regard to withdrawal from representation, a lawyer must withdraw when the lawyer knows or it is obvious that continued representation will result in a violation of a disciplinary rule, including all of the above. (DR 2-110). Thus, withdrawal is mandatory, whether the lawyer is “inside counsel” employed by the issuer or “outside counsel” retained by the issuer, when the representation would involve knowingly making a false statement, failing to disclose that which is required by law to be disclosed, or assisting the client in conduct that the lawyer knows to be illegal or fraudulent.

• We recognize that one of the most difficult areas in which to fashion a fair rule involves the situation where the attorney has not committed a fraud, has not assisted in the commission of the fraud and has not participated in the preparation of material to be used in the fraud, but still learns that the client or a third person such as an employee, director, officer or investor has perpetrated a fraud upon a third person, including the Commission itself. In that case, we subscribe to DR 7-102. If the lawyer receives information clearly establishing client fraud and the client refuses or is unable to rectify the fraud, the lawyer must reveal the fraud to the affected person, unless the information is protected as a confidence or secret. Beyond that, when a person other than the client has perpetrated the fraud upon a tribunal, which includes all adjudicatory bodies, the lawyer must reveal the fraud. (DR 7-102 [B][2]). (The issue is discussed in much greater depth in Formal Opinion No. 1990-2 by the Committee on Professional and Judicial Ethics of the Association [Feb.27, 1990]. We support the resolution of the dilemma propounded by that Formal Opinion.)

The above list is not intended to be complete or even comprehensive. It is presented merely to point out that despite some differences over the proposed rules—important to our membership—there remains a fertile and extensive landscape upon which can be built a strong set of regulations. We share a common understanding about the need for attorneys representing issuers to act not only as advocates but as members of the bar sworn to uphold the law.
Concerns

The report that follows this preliminary statement explains some of our concerns and differences with the proposed rules in greater detail. Unfortunately, given the size and diversity of our membership and the enormous number of complex issues raised by the proposed rules, we have not been able to address all that could have been covered in an appropriate comment. For example, applying the rules of practice to foreign attorneys carries with it such an extensive array of potential problems that we have deferred, for another day, comment on that issue. In that regard, while understanding that the Act required promulgation of rules within 180 days, we do not read the Act as specifically requiring any other particular rule beyond up-the-ladder reporting. Any rules which go beyond the one rule mandated by Congress could and should, consistent with the Act, be adopted with caution and reserve after a full hearing, more than a 30 day comment period, from the many groups who will be affected by the proposal. Rules regarding withdrawal, disaffirmance, documentation and disclosure do not have to be adopted in the first 180 days.

Criminal and Civil Liability

Section 307 of the Act calls for rules setting forth minimum standards for professional conduct for attorneys appearing and practicing before the Commission. Such rules, including the Model Rules, the New York Code and even the Commission’s own previous rules under 17 CFR 102, traditionally are not enforced as criminal matters. However, 15 U.S.C. § 7202, as added by the Act provides that a violation of any rule or regulation issued by the Commission pursuant to the Act shall be treated as a violation of the Securities Exchange Act of 1934, which carries criminal penalties. (15 U.S.C. § 78ff). The Commission’s release accompanying the proposed rules said that “[t]he Commission does not believe...that violations of the proposed rule would, without more, meet the standard prescribed...for the imposition of criminal penalties.” The phrase “without more” apparently refers to the fact that Sec. 78ff authorizes up to twenty years imprisonment for “willful” violations of any regulation of the Commission. In sum, a willful violation of one of the new rules is a serious criminal matter, notwithstanding the Commission’s assurances. This is not consistent with the Senate sponsors’ assurances on the Senate floor where Sen. Sarbanes asked, “Furthermore, I understand that under this amendment it can only be enforced by the SEC through an administrative proceeding. Is that correct?” To which Sen. Edwards responded, “The answer is yes. The only way to enforce this legal requirement is through an administrative process.” Congressional Record, Senate S6557.
The Commission should specifically include, within the regulations, language which guarantees that the administrative process will be the exclusive means of enforcement.

As well, although it was made clear during floor debate that the sponsors had no intention of creating civil liability for violation of the promulgated professional standards, there is no clear statement in the Act or rules establishing that protection. In light of the ensuing discussion regarding mens rea and the definitions of “appropriate response” and “material breach of fiduciary duty,” it becomes critical that the sponsor’s intent, i.e., no criminal or civil liability should attach by virtue of a professional standard violation, be clearly enunciated.

**Mens Rea—Evidence of a violation—the duty to act**

There is, and should be, a critical distinction between the responsibility of an attorney for his or her own conduct—conduct in which the attorney personally engaged such as giving advice, counseling and assisting in the preparation and filing of documents with the Commission—and conduct of others of which the attorney has only been informed. Attorneys can and should be held to a high standard with regard to their own professional activities. For example, Model Rule 1.1 requires a lawyer to act with “the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation.” That rule can apply to the services provided by the lawyer in a professional capacity. There are circumstances where the attorney’s own participation in committing a fraud or violating the law may be assessed—just as with any other person so accused—by constructive knowledge or measured by an obligation to meet an objective standard.

However, the proposed rules go well beyond regulating the personal conduct of the attorney. They assign a “watchdog” function to attorneys. Under the rules as proposed, attorneys are required to report the misconduct of others even where the attorney played no role in any of the actions that led to the violation. In other cases the attorney may have only learned of the misconduct through confidential, secret or privileged communications. In still other cases, the attorney may have a conscious awareness of the violation, being committed or having been committed by others, while not having personally engaged in any of the wrongful conduct. In some cases the attorney may only have circumstantial grounds to form a suspicion or belief

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2. Sen. Edwards, in explaining the bill, said, “One final point. Nothing in this bill gives anybody a right to file a private lawsuit against anybody. The only people who can enforce this amendment are the people at the SEC.” Cong. Record, Senate 7/10/02, S6552.
that others, including officers, employees, agents, directors or shareholders, have engaged in misconduct—but cannot be certain.

Under the proposal, the attorney is required to act based upon two determinations: Is there “evidence of a material violation?” And, was there an “appropriate response?” These “triggers” for action are measured upon an objective assessment of the information available to the attorney about misconduct by others and the conclusions that should have been drawn by the attorney.

Although we oppose mandatory disclosure, as discussed infra, if the proposed rules will continue, notwithstanding our objections, to allow the attorney no discretion, then it becomes essential that a rigorous mens rea standard be employed. An attorney should not be forced to disclose confidences and secrets, or act against the interests of the client, unless the attorney has actual awareness of essential facts and, under all the known facts and circumstances, it is clear that a material violation is continuing or is about to occur. It simply is not fair to expect an attorney to report misconduct, withdraw or disaffirm or otherwise act in the attorney’s best judgment against the interests of the client when the attorney merely has “constructive” knowledge of essential facts necessary to draw a conclusion of misconduct by others in which the attorney has not personally engaged. Unlike the situation where an attorney is accused of personal wrongdoing and it may be fair, in proving that wrongdoing, to ask what the attorney knew or should have known, here, the concept is stretched to new limits by holding an attorney accountable for conclusions he “should” have made about other actors’ wrongdoing.

The definition of “evidence” invites “Monday morning quarterbacking.” When the definitions contained in Part 205.2 (e), (k), and (l) are read in combination, as they must be, “evidence of a material violation” means “information that would lead a reasonably prudent and competent attorney, acting reasonably, to reasonably believe that a material violation has occurred, is occurring, or is about to occur.” If the definition makes any sense at all, it is dangerous. First, what constitutes “information?” Is it gossip, hearsay, innuendo, a combination of circumstances from which the attorney, in retrospect, should have drawn an inference? The proposal asks, in hindsight, “Would it have been unreasonable for a prudent, competent attorney to have concluded that there was misconduct?” The proposal shifts the burden to an attorney, facing an after-the-fact inquiry, to defend by proving the negative, i.e., to prove that the information would not have led a reasonably prudent attorney to believe that another person had engaged in wrongdoing. This is simply unfair. Rea-
sonable people, even prudent attorneys, can differ in drawing the conclusion that an officer or employee has breached a duty or broken a law. That difference of opinion cannot be turned into a basis for disciplinary sanction.

The issues and problems that arise in representing issuers require informed advice, zealous advocacy and creative solutions. Clients need to trust their lawyers, and lawyers need to feel free to give independent advice. The definitions employed by the rules to trigger investigatory action will create a world of caution, suspicion and distrust, thereby casting a pall over the attorney client relationship.

Compounding the problem, the misconduct that must be reported ("material violation") includes any breach of fiduciary duty, which can include omissions or failures to act. Therefore, an attorney will be obliged to act by reporting up-the-ladder or beyond under the rules when, in retrospect, a "prudent, competent" attorney would have had enough "information" to "reasonably believe" that another actor, be it employee or agent, failed or omitted to do something which ought to have been done.

When the New York Code mandates corrective action, it is because the lawyer "knows or it is obvious" that the attorney will be drawn into participating in misconduct. On the other hand, actual knowledge is not required when the attorney's response is discretionary. Compare "Mandatory Withdrawal" and "Permissive Withdrawal" provisions of DR 2-110. This combination of standards mandates action to which the attorney can be held readily accountable, but merely authorizes action, upon an expectation of good faith, when the circumstances or conclusions to be drawn from the circumstances are not so clear. Our concern is that the proposed rules consistently mandate action, leaving no discretion to the attorney, even where the attorney is acting in good faith and may not have actual knowledge of the information which may lead someone later, second-guessing the decision after the unforeseen has occurred, to conclude that the attorney failed to perform a required act.

Willful blindness should not be condoned. A conscious disregard of material violations is inconsistent with acting in good faith. An attorney should not be able to consciously avoid information in order to defend inaction later by claiming ignorance. However, in the absence of such a demonstration, an attorney should not face sanctions for failing to see what becomes clear only in hindsight.

*Mens rea—Appropriate Response*

Under the proposed formulation, an attorney is required to pursue a matter up-the-ladder and to the Commission (either directly or indirectly
through a QLCC) when there is not an “appropriate response.” Once again, we believe that the definition—a response that provides a basis for an attorney reasonably to believe that no material violation has occurred or that appropriate measures have been taken—invites second-guessing which is perilous to the attorney. The inevitable result will be over-caution by attorneys who, motivated by self-protection, will document and pursue matters when, in fact an appropriate response was given, but they are not in possession of enough information to make a reasoned judgment or are too frightened to accept a reasonable response. The resulting atmosphere of mistrust and doubt among attorneys and clients is counterproductive—to the point of dysfunction.

Once an attorney has reported and documented a possible violation, the attorney should be assured that good faith reliance upon the response protects the attorney against further sanction. Otherwise, the rules and an instinct for self-preservation would require an attorney to ignore or bypass higher-ranking officers, attorneys and directors even though the attorney in good faith believes that further corrective action is not required. Once again, recklessness or willful blindness is not acceptable. But in the absence of recklessness, a reporting attorney should be able to desist from further action once the attorney, in good faith, under all the known facts and circumstances, believes that appropriate corrective measures have been taken.

Confidentiality and Attorney-Client Privilege

An attorney should not be required to disclose confidential (privileged) information or client secrets without the client's consent. Privilege and client confidentiality are impinged upon by four different sets of provisions in the proposed rules: mandatory withdrawal with notification; disaffirmance, documentation and disclosure. The CityBar opposes any rules which require an attorney, over the client's objection, to withdraw, report, notify or disaffirm beyond the requirements now embodied in the New York Code. The withdrawal, notification and disaffirming requirements, discussed below, to the extent that they mandate actions against the client's interest or disclosure of confidences or secrets are unnecessary, and unwarranted, and constitute an unjustified disruption of necessary attorney-client communication.

Mandatory withdrawal

The Model Rules and the New York Code follow the same formulation with regard to withdrawal: if it is obvious that the lawyer's contin-
ued representation will result in a violation of a disciplinary rule, the lawyer must withdraw. If it is “likely” that continued representation will result in a violation of a disciplinary rule or the client persists in a course of action involving the lawyer's services that the lawyer reasonably believes is criminal or fraudulent, the lawyer may withdraw. In either event, the lawyer must take steps to avoid foreseeable prejudice to the client.

The proposed rules require a retained attorney to withdraw when the attorney has not received an “appropriate response” to a reported material violation and the violation is ongoing, or about to occur, and is likely to result in substantial injury to the financial interest of the issuer or investors. The proposed rules permit withdrawal when the attorney reported a past violation which went uncorrected, and which was likely to have resulted in substantial injury to the financial interest of issuers or investors in the past but is not ongoing. The proposed rules say nothing about taking steps to mitigate harm to the issuer. To the contrary, we believe the proposed rules would exacerbate the harm to the issuer by requiring notice that the withdrawal “is based upon professional considerations.”

As can be seen, the proposed rules are more demanding in some respects and less demanding in others. The New York Code and Model Rules only address the situation in which the lawyer's conduct or the use of the lawyer's services are at issue. The bar rules do not speak of withdrawal where the client has engaged in misconduct or persists in misconduct, but the attorney merely has notice of the misconduct and is not implicated directly or indirectly through misuse of the lawyer's services. On the other hand, the Commission's proposed rules would require attorneys who were aware of a continuing violation to withdraw, even where the misconduct was unrelated to the attorney or the attorney's services.

There are three problems with the proposed scenario:

• An attorney should not be required to abandon the client when the misconduct is unrelated to the attorney's performance. If, for example, a client wrongfully fails to disclose material information in a filing, the attorney may, in good faith, decide to stay with the client, while continuously urging compliance with the law. As long as the attorney's services are not being misused—the attorney played no role in preparing the filing - and the attorney is, personally, acting ethically, why should the attorney be forced to abandon the corporation as a client?
• An announcement to the Commission and others that the withdrawal is “for professional considerations” is a red flag—
an invitation to enforcement action and adverse litigation. Obviously, withdrawal can be accomplished quietly, without notice to anyone but the client—consistent with the obligation to protect the interests of the client.

• There may be situations where it could be argued the lawyer may or should choose to act: where the lawyer’s services were used to assist in an ongoing crime or fraud; where the lawyer needs to disaffirm the lawyer’s own work-product upon which third persons continue to rely to their potential detriment (See, ABA Comm. on Ethics and Professional Responsibility, Formal Op. 92-366); or where the lawyer seeks to prevent a crime which the client intends to commit. (EC 4-7). On the other hand, where the misconduct and the harm are things of the past and where the lawyer’s services have not been utilized to accomplish or conceal the violation, there is no justifiable reason for the attorney to notify the Commission other than to provide the SEC with information with which to commence an enforcement action, and that is insufficient reason to override client privilege.

• The proposed rules provide (Part 205.3[d][3]), “the notification to the Commission prescribed.... [upon withdrawal] does not breach the attorney-client privilege.” We think this is an unauthorized usurpation of the power to define the scope of the attorney-client privilege. As well, it confuses the privilege with disciplinary rules which also may protect client confidences. The attorney-client privilege is not a creature of professional conduct rules. It stands independently as a hybrid product of State and Federal Constitutional, legislative and common law. It is neither created, nor can it be diminished, by rules designed to regulate the profession. Congressional authorization to promulgate standards of conduct for professional practice before the Commission cannot support a claim that the proposed rules now override Fed. Rules of Evidence 501, or the Constitution or State authority. Consistent with the Act, one could argue that the Commission can create disciplinary rules governing practice before the Commission which forgive, in the course of that practice, or provide safe harbor to, an attorney who has violated rules of confidentiality established within Part 205. We do not believe Section 307 “impliedly” gives an enforcement agency the right to define privileges.

Disaffirmance
The New York Code permits disaffirmance, without more, of a writ-
ten or oral representation or opinion by the attorney, which the lawyer has come to learn was based on materially inaccurate information. If the representation or opinion is still being relied upon or is being used to further a crime or fraud, the disaffirmance can be done over the client's objection. Confidences or secrets may be revealed to the extent implicit in withdrawing the document. As well, the attorney may reveal the intention of the client to commit a crime and information necessary to prevent the crime. If the inaccurate representation by the lawyer is not currently being used to commit a crime and is no longer relied upon by others, then the lawyer can rectify the error, but cannot reveal confidences or secrets.

The proposed rules would permit disaffirmance to rectify past harm even where confidences and secrets would be revealed. The proposed rules would also mandate disaffirmance where the violation is ongoing or about to occur and is likely to result in substantial injury to the financial interest or property of the issuer or of investors. We think this goes too far. There are occasions when a lawyer and the client prepared a document for filing, which was believed to be true at the time of the filing. If later events render the document false, the lawyer should not be permitted, over the client's objection and to the client's detriment, in the name of rectifying the past wrong, to disaffirm the document while revealing client confidences.

Documentation
We are concerned that the documentation requirements are impractical and will threaten the free flow of ideas and candid conversation between attorney and client as well as between attorneys. Since there is a risk that documents will find their way into court proceedings, be they criminal or civil, the requirement that they be made contemporaneously and preserved will stultify ordinary communications, which are a necessary part of any successful venture. As a practical matter, both sides to a conversation will protect their position by excessive documentation. In turn, CEOs or CLOs may soon find themselves mandating review and collection of all documentation created pursuant to the rules. It is unlikely that this will produce the desired result—honest compliance with the law.

Safe Harbor for Chief Legal Officers
A CLO who has been advised of a past, present or future material violation may conduct an inquiry or ask the QLCC to conduct the in-
quiry. However, if the CLO believes that the issuer has failed to take remedial measures directed by the QLCC to stop any material violation that is occurring, to prevent any material violation that is about to occur and/or has failed to rectify a past material violation, then the CLO must go outside the company to disaffirm, in writing, any documents that have been submitted or filed with the SEC that the CLO reasonably believes are false or materially misleading.

The proposed rules do not appear to give a CLO the same safe harbor provision afforded other attorneys. Part 205.3(c)(1) declares that an attorney who has reported a violation to a QLCC has satisfied the attorney’s reporting obligations. However, the same section creates an exception: the provisions of 205.3(b)(3) requiring a CLO to report the failure of the issuer to take remedial measures demanded by the QLCC still apply. As well, 205.2(j)(5) make it clear that the CLO, the highest ranking attorney within the organization, must personally notify the Commission and disaffirm filings when the issuer has failed to comply with the QLCC’s directives. In contrast, the rules should provide safe harbor to a CLO who submits information to the QLCC.

The obligation to go outside of the organization instead of up-the-ladder is significantly different than the duty imposed upon other attorneys. First, the CLO is required to disaffirm any writing or document submitted or filed by the issuer with the Commission which the CLO reasonably believes to be false or materially misleading. Other attorneys are only obligated to disaffirm documents that they prepared or assisted in preparing. The CLO, however, must disaffirm all false documents, from whatever source, including documents and filings the CLO never prepared. How will the CLO know which documents are false? Since the initial report and request for inquiry works its way up to the CLO or the QLCC and CLO, the result is that the CLO hears all or most claims calling into question any documents which are filed with the Commission during the internal up-the-ladder process. Thereafter, if the CLO is required to disavow documents the CLO “reasonably believes” to be false, the CLO will in effect be called upon to disclose a large number of documents that the CLO reviewed during an inquiry.

Secondly, other attorneys are mandated to disaffirm documents they prepared when the violation is ongoing or about to occur. There is no obligation to report past false filings where there is no ongoing violation. On the other hand, the CLO is required to report to the Commission past violations as well as ongoing and future violations.

Finally, the CLO is required to report a failure to rectify past viola-
tions, or the existence of present or future violations, without regard to any consideration of whether the violation is likely to result in substantial injury to the financial interest or property of the issuer or investors.

In sum, upon an issuer’s failure to comply with a QLCC directive, the CLO is mandated to notify the Commission of past, present and future violations of which the CLO learned and which have not been rectified or prevented by the issuer regardless of whether there is a risk of ongoing or future injury to the issuer or investors. The CLO must then disaffirm, to the Commission, all false or materially misleading documents submitted by the client, whether prepared by the CLO or submitted by others—even in circumstances where the disaffirmance may harm the issuer or its investors. We believe this goes too far.

The CLO is the attorney closest to the Board and the CEO. The CLO is in a position to know the most important and private confidences and secrets of the client. The CLO’s obligation or authority to reveal confidences and secrets should be limited to those situations authorized by the New York Code. The issuer and the CLO should be permitted to prevent disclosure of past misconduct of which the CLO became aware in confidence.

“Breach of Fiduciary Duty”

The definition of “breach of fiduciary duty” (Part 205.1[d]) is confusing and a trap for the unwary. It is unreasonable to expect an attorney to become familiar with the various common law and statutory definitions of fiduciary duty in 51 jurisdictions. We propose that the breach should be measured by the governing body of law in the jurisdiction of incorporation. It should also be made clear that duty is that owed by the officers and directors to the issuer and the shareholders only.

“Representation of an Issuer”

The definition, Part 205.1(f), should not include attorneys acting “for the benefit of an issuer,” as this would include attorneys having no attorney-client relationship with the issuer. It is sufficient to refer to attorneys who are engaged or retained to act in their capacities as an attorney for the issuer, or to provide legal services to the issuer. Otherwise, attorneys who work for underwriters, banks, financial advisors, etc., all of whom owe separate duties to actors other than the issuer, will inadvertently find themselves governed by a whole new set of practice regulations.

“Appearing and Practicing”

There is no sound reason, and it is unfair, to include attorneys who
are adverse parties in enforcement or administrative proceedings within the reporting and withdrawal requirements of the proposed rules. The attorneys in that situation are performing traditional adversarial advocacy roles. It is untenable to place them in the position of enforcing the law against clients they are defending in an enforcement action.

Attorneys who merely give advice against the need to file are not appearing or practicing before the Commission and should not be included. If an attorney never comes into contact with the Commission, the Commission should not claim authority to regulate the attorney's conduct. It is impractical for the commission to attempt to extend control over professional conduct beyond contact with the agency. The agency can properly review the client's decision to file or fail to file, but private consultations in remote places that may have factored into that decision cannot be deemed to constitute “practicing” before the agency.

Who's the client?

The Model Rules and the New York Code make it clear that the client is the organization and not any of its constituents. It is inconsistent and inviting conflict to ask the attorney to represent both the issuer and the investors, when their interests, which may overlap, do not always coincide.

Best Interests

Part 205.3 mistakenly states that an attorney “shall act in the best interest of the issuer and its shareholders.” (emphasis added) The addition of this phrase subverts the basic principle recognized both in the New York Code and the Model Rules that the attorney represents the issuer and not any of its constituents. We believe that this single provision of the proposed rules will spawn a set of conflicting and competing governing principles that will lead to unintended liability and lawsuits for breach. Corporate officers and directors have a fiduciary duty to shareholders to act in their best interest. Under the business judgment rule, as long as they have performed that task with independence, disinterest, good faith and diligence, they are protected from personal liability. Directors look to maximize investment security, stability and profit. On the other hand, attorneys have an entirely different set of governing principles. They are bound to perform with diligence, competence and loyalty; they owe a duty of confidentiality. They give legal advice, but attorneys do not run the company and do not make the client's decisions. They are not in a position of governing responsibility, they do not have an officer or director's immunity and they should not be exposed to liability for lapses in governance.
Subordinate Attorneys

The proposed rules impose an artificial hierarchy of supervisory and subordinate attorneys and unnecessarily impose separate duties upon them. Law firm structures come with wide variety. It is an incorrect assumption that firms are structured as viewed in the regulations. For those firms that do have subordinates and supervisors working on behalf of a client, the rules would interfere with the collaborative nature of the professional relationship. Subordinates would pass problems up to supervisors without attempting to solve them. Supervisors would be artificially forced to make decisions which more naturally should be delegated or shared by a team effort. There is no legitimate justification for rules creating separate categories of attorneys within a firm. It is sufficient to hold attorneys who have ultimate responsibility for a decision accountable for their own decision making.

Conclusion

The Citybar appreciates the effort and good intentions that underlie the proposed rules. We recognize that the Commission staff had time constraints as it undertook a project of enormous complexity. Our Association is committed to working with the Commission on this project. We represent nearly 22,000 members, many of whom can lend experience and knowledge to the highly technical and difficult task before the Commission. To the extent that the report that follows might appear critical of the Commission’s effort, we reiterate that we share the Commission’s goal—demanding honest and faithful service from attorneys who represent issuers. We believe the Commission can write rules to achieve that objective and we appreciate the opportunity to work with you to accomplish it.

REPORT OF THE TASK FORCE

The Association of the Bar of the City of New York Supports the Promulgation of Regulations Implementing Section 307 that are Consistent with the Model rules and the New York Code of Professional Responsibility

The fiduciary relationship between clients and their attorneys provides sufficient comfort to clients to make them feel free to share any

3. Representatives of five committees of the Association of the Bar for the City of New York worked to assemble this response for presentation to the Executive Committee. The committees so represented were: the Professional Responsibility Committee, the Professional Discipline Committee, the Securities Regulation Committee, the Professional & Judicial Ethics Committee and the Corporation Law Committee.
information that the attorney may need in order to advise the client on compliance with the securities laws. This may include notifying the client that past conduct may have constituted a violation of the securities laws and may require disclosure and/or other remedial action, or notifying the client that some contemporaneous action or planned conduct by an officer, employee or agent of the issuer may lead to a violation of the securities laws and should be stopped before such violation occurs.

Both the Model Rules and the New York Code have recognized that attorneys may be in a unique position to learn of misconduct and to advise their clients appropriately. Therefore, both the Model Rules and the New York Code have prescribed the action that lawyers should take when they learn that an officer, employee or other person associated with the organization has acted, intends to act (or refuses to act) in a manner that constitutes a breach of an obligation to the organization or a violation of law that may be imputed to the organization, and that the conduct is likely to result in substantial injury to the organization. Each prescribes that the lawyer in these circumstances should consider:

- asking for reconsideration of the matter,
- advising that the organization obtain a separate legal opinion for presentation to the appropriate authority in the organization, or
- referring the matter to the highest authority within the organization.

Each also prescribes that if, despite these efforts, the highest authority in the organization insists on acting (or refuses to act) in a way that “is clearly a violation of law and is likely to result in substantial injury to the organization,” the lawyer may withdraw in accordance with the Model Rule 1.16 or DR 2-110, respectively.\(^4\)

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4. Model Rules of Professional Conduct 1.13; Code, DR 5-109. Indeed, we believe that Section 307 merely reinforces existing obligations governing the conduct of New York attorneys under DR 5-109 and other disciplinary rules in the Code. See, e.g., DR 4-101(C)(5) (permitting lawyers to reveal confidences or secrets to the extent implicit in withdrawing a written or oral representation previously given by the lawyer where the lawyer discovers that it was based on materially inaccurate information or is being used to further a crime or fraud); DR 7-102(D) (requiring a lawyer who receives information clearly establishing that the client has perpetrated a fraud upon a person or tribunal to call upon the client to rectify same, and if the client refuses, to reveal the fraud to the person or tribunal except where the information is protected as a confidence or secret).
Moreover, we believe that the response of issuer’s counsel to evidence of misconduct that may be attributed to the issuer under either the Model Rules or the New York Code is consistent with the course of conduct prescribed under Section 307. Attorneys who represent issuers have an obligation to act in the best interests of the issuer. When such attorneys become aware of misconduct by officers, employees or other agents of the issuer, or material misstatements made by these persons, the attorneys have an obligation to act to correct the situation within the organization, which includes disclosing the conduct “up the ladder” within the organization to the chief legal officer, chief executive officer, and/or to board members. Further, though not specifically authorized under Section 307, we believe that the Commission has the right to regulate the conduct of attorneys who appear before it to ensure that these attorneys adhere to professional rules of conduct, do not engage in or assist in unlawful or fraudulent conduct, do not knowingly submit or allow others to present false information to the Commission, and withdraw from employment where failure to withdraw will cause the attorney to violate the law or state disciplinary rules.

Proposed Part 205, however, far exceeds the above-stated premise and the authority granted to the Commission by Congress in the Act. The Act is the first federal statute that Congress has enacted and the President has signed that affirmatively mandates regulation of attorney conduct by a federal agency on a national basis. The pertinent language in Section 307 authorizes the Commission to set forth “minimum standards of professional conduct for attorneys appearing and practicing before the commission in any way in the representation of issuers.” Rather than setting forth “minimum standards,” proposed Part 205 sets forth standards far beyond those set forth under the Model Rules and the ethical codes in each state, and in some instances is inconsistent with federal and state case law.

We understand that the Commission has prepared this rule, which has far-reaching consequences, while working under extreme time pressure. Given the complexity of the subject matter, the nascent state of the public debate of the statute, the brevity of the period available for analysis, and the limits of our predictive capacities, we recommend that the Commission meet its statutory obligation by enacting a simplified rule, such as the one contained in the appendix, on January 26, 2003, and leave the balance of the proposed rules for more considered comment and discussion over a longer period of time. Accordingly, this letter is limited to:
i. discussing how the proposed rule modifies the attorney-client privilege and may be contrary to state and federal law;

ii. discussing the negative impact of the proposed regulation on the attorney-client relationship;

iii. discussing the proposed extension of the Act's reach beyond those attorneys prescribed and anticipated under Section 307;

iv. commenting on the role of the QLCC;

v. discussing adding a "safe harbor" for the chief legal officer;

vi. discussing the proposed sanctions against attorneys;

vii. discussing questions raised by terminology used in the proposed Act;

viii. discussing our support for the promulgation of rules consistent with Section 307, the Model Rules and the New York Code of Professional Responsibility, and presenting a proposed rule that may be enacted on January 26, 2003.

DISCUSSION

I. The Proposed Rules Modify the Attorney-Client Privilege

An area of primary concern for the CityBar is with the “noisy withdrawal” provisions of proposed Section 205.3. Section 205.3(d) prescribes instances in which a reporting attorney who has not received an “appropriate response” from the issuer within a reasonable time is either required or permitted to report otherwise privileged information relating to a suspected material violation to the Commission. Section 205.3(d)(1) mandates that an attorney retained by the issuer who (1) has reported evidence of a material violation up-the-ladder and has not received an appropriate response in a reasonable time, and (2) believes that a material violation is ongoing or about to occur and likely to result in substantial injury to the financial interest or property of the issuer or investors, to withdraw from the representation of the issuer, provide notice of withdrawal “based on professional considerations” to the Commission, and disaffirm any document submitted to the Commission that the attorney assisted in preparing that the attorney reasonably believes may be materially false or misleading (the same section provides that the reporting attorney who is in-house counsel need not withdraw from the representation).5

5. Under the Model Rules and the New York Code, a lawyer in the same situation would be permitted to withdraw, and may disclose the intent of the client to commit a crime and that.
Section 205.3(d)(2) permits a reporting attorney who reasonably believes that a material violation has occurred and likely has resulted in substantial financial injury to the issuer, but does not believe the violation is ongoing, to disaffirm any tainted submission to the Commission, withdrawing from representing the issuer and providing notice to the Commission of his or her withdrawal “based on professional considerations.” In the Commission release describing proposed Part 205, the Commission acknowledges that “[p]roviding notification to the Commission . . . goes beyond what the Act expressly directed the Commission to do.” SEC Release 33-8150.

The external reporting rules proposed by the Commission conflict with the principle recently reaffirmed by the United States Supreme Court that the integrity of the attorney-client privilege takes precedence over unauthorized disclosure except in very limited circumstances. In Swidler & Berlin v. United States, 524 U.S. 399, 118 S.Ct. 2081 (1998), the Court, rejected the government’s effort to create a new exception to the privilege which would allow disclosure by an attorney of privileged client communications after the death of the client to a grand jury conducting an investigation into alleged criminal wrongdoing. The Court stated that the purpose of the privilege is “to encourage full and frank communications between attorneys and their clients and thereby promote broader public interest in the observance of law and the administration of justice.” 524 U.S. at 403, 118 S.Ct. at 2084 (internal quotations omitted). Thus, the Court held that a client’s confidence that his or her discussions with counsel would remain privileged was of paramount importance in the administration of justice. That importance “justified” “the loss of evidence admittedly caused by the privilege . . .” even in grand jury investigations. 524 U.S. at 408, 118 S.Ct. at 2086. We believe that the “noisy withdrawal” provisions of proposed 17 C.F.R. 205.3 would erode the duty of loyalty in a far more serious manner than the breach of the privilege that the Supreme Court rejected in Swidler & Berlin.

The modification of the attorney-client privilege is governed by Rule 501 of the Federal Rules of Evidence, which states, in relevant part, that:

Except as otherwise required by the Constitution of the United States or provided by Act of Congress or in rules prescribed by the Supreme Court pursuant to statutory authority, the privilege of a witness, person, government, State, or political subdi-

information necessary to prevent the crime. See Model Rule 1.13; NY Code, DR 5-109, DR 4-101(C).
vision thereof shall be governed by the principles of the common law as they may be interpreted by the courts of the United States in the light of reason and experience.

Thus, the Federal attorney-client privilege can be modified only by a judicial constitutional ruling, by an Act of Congress or through the Supreme Court's rule-making authority. The external reporting rules proposed by the Commission are being promulgated solely upon the Commission's rule-making authority and Section 307 of the Act, which, while directing the Commission to "issue rules, in the public interest and for the protection of investors, setting forth minimum standards of professional conduct for attorneys appearing and practicing before the Commission," does not provide authority to the Commission to change the attorney client privilege Rule. Thus, we believe that the proposed rules are not propounded in a manner authorized by Rule 501. As such, the external reporting rules are beyond the Commission's rule-making authority, and will be a nullity if formally promulgated.

Further, it is entirely unclear that the Commission can supersede state ethical rules governing the attorney-client privilege and the attorney-client relationship in the manner suggested by proposed Part 205 and the Commission release. The release states that

a commission rule permitting disclosure would appear to preempt a state's rule forbidding disclosure. Accordingly an attorney appearing and practicing before the Commission who is admitted in a jurisdiction that forbids disclosure of confidential information under circumstances where the proposed rule would permit disclosure, may disclose the information to the Commission, notwithstanding the contrary state rule.

SEC Release No. 33-8150. There is nothing in Section 307 to suggest that Congress authorized the Commission to preempt state law and rules governing attorney conduct. On the contrary the states are the primary regulators of attorney conduct, and the relationship between attorneys and clients. The proposed external reporting rules are in conflict with the Model Rules (which have been adopted by most states) and the New York Code. Assuming that the Commission could validly promulgate these rules, there would be serious questions regarding whether the Commission rules could "trump" conflicting state ethics rules (see In the Matter of John Doe, Esquire 801 F. Supp. 478 (D. NM 1992)) and whether the new disclosure/non-waiver rules would protect any disclosure to the Commission of privileged
information from third parties who would argue that the privilege no longer attaches (see In re Subpoenas Duces Tecum, 738 F.2d 1367 (D.C.Cir.1984)).

In addition, the external reporting provisions are inconsistent with the legislative history of the Act. The legislation which mandates the creation of Rule 205 is contained in §307 of the Act. Section 307 was proposed as an amendment to the Act by, among others, Senators Edwards and Enzi. In discussing the proposed amendment, Senator Sarbanes, the sponsor of the legislation, questioned Senator Edwards concerning whether the amendment would impose any duty on attorneys to notify the SEC of a violation. The following colloquy appears in the congressional record (148 Congressional Record S6524, p. 95):

“Mr. SARBANES: It is my understanding that this amendment, which places responsibility upon the lawyer for the corporation to report up the ladder, only involves going up within the corporation structure. He doesn’t go outside of the corporate structure. So the lawyer would first go to the chief legal officer, or the chief executive officer, and if he didn’t get an appropriate response, he would go to the board of directors. Is that correct?

Mr. EDWARDS: Mr. President, my response to the question is the only obligation that this amendment creates is the obligation to report to the client, which begins with the chief legal officer, and, if that is unsuccessful, then to the board of the corporation. There is no obligation to report anything outside the client the corporation.” [Emphasis supplied]

Senator Enzi was also at pains to point out during the debate that the legislation would impose no duty on attorneys to report to the SEC. Senator Enzi noted (148 Congressional Record S6524 at p. 90):

“In the wake of Enron, over forty professors with expertise in Federal securities and ethics law, have written to SEC Chairman Harvey Pitt asking for some form of regulation over the practice and conduct of attorneys involved in Federal securities law.

In their letter, they state that if senior managers will not rectify a violation, lawyers who are responsible for the corporations’ securities compliance work, should be required to report to the board of directors.

As they point out, such a disclosure obligation is still less onerous than that imposed on accountants under section 10A of the 1934 Securities Exchange Act, which requires an auditor to
report, both the client's directors and simultaneously to the SEC, and illegal act if management fails to take remedial action.

The amendment I am supporting would not require the attorneys to report violation to the SEC, only to corporate legal counsel or the CEO, and ultimately, to the board of directors.

Some argue that the amendment will cause a breach of client/attorney privilege, which is ludicrous. The attorney owes a duty to its client which is the corporation and the shareholders. By reporting a legal violation to management and then the board of directors, no breach of the privilege occurs, because it is all internal within the corporation and not to an outside party, such as the SEC.” [Emphasis supplied]

Since the founding of the Republic, the states have fiercely asserted and preserved for themselves the primary and principle role in the regulation of lawyers. That continues to hold true. We note, for example, that Judge Judith S. Kaye, President of the Conference of Chief Justices, commenting upon the proposed rules on behalf of the Conference, recently wrote, “In our view, the expansive approach now proposed by the Commission for the regulation of the ethics of lawyers, as set forth in these proposed rules, is radically inconsistent not only with principles of federalism but also with historic Commission policy.” Letter to Jonathan G. Katz, Secretary, SEC by Hon. Judith S. Kaye, Dec. 13, 2002. In the past, Federal court encroachment has been limited to asserting rights to determine admission to practice and to disciplining lawyers who appear before them, and federal agencies have established regulatory authority over lawyers conducting business before them. In each instance, the regulation has been narrowly tailored to encompass only lawyers having direct dealings with the court or agency. Indeed, before Sarbanes-Oxley, the only prior intervention by Congress in the arena of regulation of lawyers was the so-called “McDade Amendment” passed in 1999, in which Congress enforced the states’ right to apply their respective versions of the no-contact rule (Model Rule 4.2) to federal government lawyers over the strident objections of the Department of Justice, which sought to exclude the enforcement of the no-contact rule against federal prosecutors. In keeping with federal, state, and Congressional legislative precedent, we believe that the Commission should not promulgate rules that affect an issue so fundamental to state legislation as the attorney-client privilege and attorneys' duties to preserve client confidences.
We recognize that, in certain rare circumstances, adherence to the privilege might prevent the Commission from learning of a violation which an issuer has determined not to self-report, notwithstanding an attorney’s advice. We believe, however, that current rules which permit an attorney to gain a client’s trust, to learn of potential wrongdoings or client failures and to encourage compliance are, as a practical matter, more effective in the long run than a rule that discourages confidential communication. The salutary effect of preserving the attorney-client privilege—encouraging disclosure by an issuer to its attorney of any possible violations—more than outweighs any hypothetical detrimental impact.6

A. Limited Waiver and Proposed 17 C.F.R. 205.3(e)(3).

Section 205.3(e)(3) of the rules proposes the potentially beneficial principle that an issuer’s disclosure of privileged information to the Commission under a confidentiality agreement results in only a limited waiver, and thereby preserves the attorney-client and work product privileges in, for example, subsequent litigation brought by private plaintiffs in federal court. Plainly, the proposed section benefits both the Commission, in granting the Staff access to information that may allow the Staff to conduct investigations much more expeditiously, and issuers, who may have wished to share privileged information with the Staff, but have been prevented from doing so by concerns over a possible general waiver. But in enacting Sarbanes-Oxley, Congress did not confer authority upon the Commission to promulgate a limited waiver rule. Thus, the rule’s validity rises or falls solely upon the strength of the Commission’s rule-making authority. Unfortunately, it is unclear that, standing alone, the Commission’s rule-making authority suffices for this purpose.7

For any rule affecting privilege to bind litigants in subsequent federal court proceedings, the rule must pass muster under Rule 501 of the Federal Rules of Evidence. Because the proposed limited waiver rule lacks any Congressional imprimatur, to be effective, the proposed rule must then accord with the “principles of common law” as interpreted by the federal courts.

6. This is not to say that attorneys are free, under state ethics rules, to assist an issuer client in perpetuating an ongoing fraud. Ethical rules already mandate that where an attorney learns that a client has committed a fraud, that the fraud is of an ongoing nature, and the client has refused to correct the fraud, the lawyer should resign. Further, where a document has been circulated publicly which contains an express or implied representation by an attorney which the attorney subsequently learns is materially false or misleading, the lawyer should disclaim such representation.

7. This concern also applies to proposed Sections 205.3(d)(1)(i) and 205.3(d)(3).
But, as the proposing release acknowledges (fn. 75), the federal case law on limited waiver is “in a state of hopeless confusion.” Indeed, a review of the relevant authorities suggests that only a minority view upholds the doctrine of limited waiver, even in the presence of a confidentiality agreement.

The concern over whether the proposed limited waiver rule rests on an adequate foundation is highlighted by the clash between the Commission’s present position that its rule-making authority suffices, and the Commission’s position in 1984 that the Commission requires specific Congressional authority to promulgate a limited waiver rule. Although nowhere mentioned in the 93-page proposing release, in 1984 the Commission requested that Congress adopt a new Section 24(d) of the Securities Exchange Act authorizing the rule. Indeed, in the Commission’s statement in support of proposed Section 24(d), the Commission pointed to a similar piece of specific Congressional legislation, the Antitrust Civil Process Act, 15 U.S.C. §§ 1311, et seq., providing that, under certain circumstances, producing privileged information to the Antitrust Division does not waive privilege. Moreover, Congress apparently rejected proposed Section 24(d).


9. Compare In re Columbia/HCA Healthcare Corp. Billing Practices Litig., 293 F.3d 289 (6th Cir. 2002), (rejecting limited waiver of both attorney-client and work product privileges, even with a confidentiality agreement); Bowne of New York City, Inc. v. AmBase Corp., 150 F.R.D. 465, 480 (S.D.N.Y. 1993) (holding that “even if the disclosing party requires, as a condition of disclosure, that the recipient maintain the materials in confidence, this agreement does not prevent the disclosure from constituting a waiver of the privilege; it merely obligates the recipient to comply with the terms of any confidentiality agreement”); Westinghouse Elec. Corp. v. Republic of Philippines, 951 F.2d 1414, 1427 (3d Cir. 1991) (stating that “under traditional waiver doctrine a voluntary disclosure to a third party waives the attorney-client privilege even if the third party agrees not to disclose the communications to anyone else”); with In re Leslie Fay Ch., Inc. Sec. Litig., 161 F.R.D. 274, 284 (S.D.N.Y. 1995) (rejecting claim of waiver where “disclosures [to USAO] were made pursuant to confidentiality agreements intended to preserve any privilege applicable to the disclosed documents); In re Steinhardt Partners L.P., 9 F.3d 230, 236 (2d Cir. 1996) (stating that disclosure of privileged information to the government may not constitute a waiver if the government agreements to maintain the confidentiality of the disclosed materials); Permian Corp. v. U.S., 665 F.2d 1214 (D.C. Cir. 1981) (limited waiver upheld with respect to work product); Diversified Industries Inc. v. Meredith, 572 F.2d 596 (8th Cir. 1978) (en banc) (no waiver of either privilege), but see In re Grand Jury Proceedings Subpoena, 841 F.2d 230 (8th Cir. 1988) (finding selective disclosure inconsistent with privilege claim and questioning Diversified).


11. See Westinghouse, 951 F.2d at 1425 ("Congress rejected an amendment to the Securities Exchange Act that provided that, under specified circumstances, providing privileged information to the government does not waive privilege, and the Commission requested that Congress adopt such an amendment in 1984").
In addition, the scope of the confidentiality agreement that the Staff would enter into under Section 205.3(e)(3) is not defined. This is important not only because issuers need to know in advance the protection that the privileged information will receive, but also because the more the confidentiality agreement allows exceptions, the more likely that a general, rather than a limited, waiver may ultimately be found.

As a threshold matter, it does not appear that the confidentiality agreement would be “so ordered,” so the agreement would remain a private agreement between the Commission and the issuer. This calls into question its effectiveness against later compelled disclosure. As well, what restraints would the confidentiality agreement impose on the Staff? For example, if the Staff concludes that the privileged information contains evidence of securities law violations, no guidance is offered as to whether the Commission, over issuer objection and notwithstanding the confidentiality agreement, may file a complaint and publicly disclose the privileged information. Guidance is similarly lacking about the restrictions, if any, the confidentiality agreement would place on the Staff’s ability to share the privileged information with other federal and state agencies, Congress, the self-regulatory organizations, civil litigants (pursuant to subpoena) and others listed in the Commission’s disclosure form as routine recipients of information provided to the Commission.\(^\text{12}\)

If the confidentiality agreements are not binding upon the Commission and are not enforceable against third parties, then they have little utility and pose great potential peril for the parties to the agreement.

III. THE PROPOSED REGULATION WILL HAVE A NEGATIVE IMPACT ON THE ATTORNEY-CLIENT RELATIONSHIP

The proposed rules represent a substantial encroachment on the attorney-client relationship because, as discussed above, they may significantly erode the attorney-client privilege.

A client must feel free to discuss anything with his or her lawyer and a lawyer must be equally free to obtain information beyond that volunteered by the client.\ldots The observance of the ethical obligation of a lawyer to hold inviolate the confidences and secrets of a client not only facilitates the full demand and Exchange Act of 1934, proposed by the Commission, that would have established a selective waiver rule regarding documents disclosed to the agency”).

\(^{12}\) See SEC Form 1662.
velopment of facts essential to proper representation of the client but also encourages non-lawyers to seek early legal assistance.¹³

The privilege exists “to protect not only the giving of professional advice . . . but also the giving of information to the lawyer to enable him to give sound and informed advice.”

The proposed rules will have the contrary effect on attorney-client communications. For example, Section 205.3(b) states that, “[a]bsent exigent circumstances, the attorney [reporting a violation] is obligated to take reasonable steps to document his or her reports, as well as any response received . . . .” Such documents “will protect the attorney in the event his or her compliance with the proposed rule is put in issue. . . .” Those documents, prepared in the press of circumstances, upon less than complete information, and motivated by an instinct for self-protection may protect the lawyer only at the client’s expense by serving as productive litigation fodder against the client. In fact, the rules make clear to issuers that their attorneys may be obligated to report any suspected misconduct to the Commission when the attorney disagrees with the company’s response. Thus, any communications with the company’s attorney relating to the potential violation, and possibly other privileged communications, may ultimately be disclosed to the Commission and may eventually form the basis of private lawsuits filed against the issuer.

Attorneys act as advocates and advisors to their clients. Unlike accountants, their role is not to “attest” to information, “certify” information or vouch to the public. Nor are they employed to enforce the law or regulations governing their issuer clients. Unlike an auditor whose very role is to be skeptical and utterly independent, an attorney acting as an advocate must be able to make full use of the attorney-client privilege (consistent with the crime-fraud exception) to make effective and zealous advocacy possible. Despite this basic understanding of the attorney’s role, the proposed rules attempt to transform attorneys into investigators of their clients, and put attorneys in the impossible position of simultaneously acting as advocates and unilateral judges of even past misconduct by the issuer and whistleblowers, rendering practically impossible the mandate that attorneys must zealously represent their clients.

A likely consequence of this erosion of privilege is that corporate officers or employees may not turn to lawyers for advice in situations where

¹³. NY Code, EC 4-1.
legal advice may, if obtained, have benefited the corporation and its shareholders. Another likely consequence is that, when a corporation turns to a lawyer for advice, it may, in light of the lawyer’s new obligation to report the client’s transgressions, limit the information it provides to its counsel upon which to formulate such advice. This chilling of communications between attorneys and clients, causing issuers to act without legal advice or to act upon legal advice rendered upon more limited information, will likely undermine the attorney’s ability to gather the relevant facts and advise the issuer as to appropriate conduct with respect to disclosures that should be made to the public or actions that should be taken to remedy material misconduct by an agent of an issuer. As the Supreme Court reminds us, a limitation upon the attorney-client privilege in the corporate context

not only makes it difficult for corporate attorneys to formulate their advice when their client is faced with a specific legal problem but also threatens to limit the valuable efforts of corporate counsel to ensure their client’s compliance with the law. In light of the vast and complicated array of regulatory legislation confronting the modern corporation, corporations, unlike most individuals, constantly go to lawyers to find out how to obey the law . . . .14

Thus, the proposed rules, part of an effort to further compliance with law by public companies, may, as a consequence, have precisely the opposite effect.

IV. THE REGULATION SHOULD PROVIDE A NARROW DEFINITION OF “ATTORNEY” WHOSE CONDUCT IS GOVERNED BY PART 205

The Commission acknowledges that the proposed rule “is broad enough to include attorneys who do not serve in the legal department of an issuer or do not act in their capacities as attorneys, but who either transact business with the Commission or assist in the preparation of documents filed with or submitted to the Commission.” Thus, for example, an investment banker or executive for an issuer who fortuitously also happens (perhaps as of many years ago) to have been “admitted, licensed, or otherwise qualified to practice law in any jurisdiction, domestic or foreign” [Section 205.2(c)]—but who in no fashion engages in the “professional

14. Id. at 593 (citations and internal quotations omitted).
conduct” of an “attorney”—would be within the scope of the proposed rule if s/he were “participating in the process of preparing any statement, opinion, or writing which the attorney has reason to believe will be filed with or incorporated into any registration statement, notification, application, report, communication or other document filed with or submitted to the Commissioners, the Commission, or its staff.” Section 205.2(a)(4).

Surely, this goes beyond what Congress was trying reasonably to achieve. First, Section 307 aims to have the Commission regulate the “professional conduct” of “attorneys” in their “representation” of issuers, not the non-professional conduct of those whom the Staff themselves acknowledge “do not act in their capacities as attorneys.” Second, the very broad “participating in the process of preparing” standard [§ 205.2(a)(4)] is already fraught with problems for attorneys actually involved in the representation of issuers, as the Staff members themselves acknowledge (stating that “Comment is also particularly invited on the breadth of ‘participating in the process of preparing’ in paragraph (a)(4) and whether the ‘has reason to believe’ standard in that paragraph is too high or too low”). Third, the proposed rule’s broad sweep, to include non-lawyers (which the Staff characterize as those who “do not act in their capacities as attorneys”), is internally inconsistent with the very next phrase in the definition of “attorney,” which extends to one “who holds him or herself out as admitted, licensed, or otherwise qualified to practice law.” Section 205.2(c) (emphasis added).

It is beyond the scope of this comment (given the very limited time available) to discuss, but nonetheless should be noted, that the proposed rule’s extension to foreign attorneys is also fraught with problems and appears to go well beyond what Congress was seeking. Determining what would constitute an “attorney” and the practice of law in foreign jurisdictions will often be difficult. Moreover, practical concerns for both international regulatory comity and material differences in various foreign jurisdictions’ respective corporate governance and reporting structures auger

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15. For example, attorneys regularly are called upon to respond to so-called “audit inquiry letters” which can call for highly technical responses. The inability to assess the potential outcome of threatened (or even pending) litigation frequently leads to a response that may or may not eventually make its way into a filing/submission to the Commission. The Staff’s proposed rule makes it most difficult for attorneys in their representation of issuers to not only formulate meaningful responses, but also to have “reason to believe” that such a communication will ultimately be communicated on to the Commission. A fortiori, imposing such legal analyses on executives who “do not act in their capacities as attorneys” would only create a trap for the unwary and not materially better inform shareholders or the investing public.
against the effort to extend the proposed rule to foreign “attorneys.” The desirable statutory objective of enhancing the responsibility of attorneys to their issuer clients will inevitably lead multinational law firms and companies to establish more efficient, internal communications structures. But that is quite different than the sort of unilateral extension to foreign “attorneys” that the Commission’s proposed rule would have.

A. Proposed Part 205 Should Be Modified To Clarify Which Attorneys Will Be Deemed To Represent An Issuer In Practice Before the Commission

In addition to the above examples of attorneys who are not engaged in a professional capacity as lawyers and foreign lawyers to whom the rule should not be applied, there are several other category of lawyers who, while employed in a professional capacity, should nonetheless be exempt from the application of the rule, including a lawyer who is “acting in any way on behalf, at the behest, or for the benefit of an issuer, whether or not employed or retained by the issuer.”

The broad sweep of this definition would include lawyers who are retained by another party, separate from the issuer, in a transaction, such as an underwriting, which is for the benefit of the issuer. This excessively broad application of the rule does fundamental damage to the attorney-client relationship, may require the disclosure of confidences of clients who are not themselves the issuer and, at a minimum, inappropriately divides the loyalty of a lawyer between his actual client and the issuer on the other side of the transaction.

Of equal concern, is the inevitable harm that the rule will cause in the relationship between attorneys within a firm - those who are responsible for the securities practice in representing an issuer and those who provide specialized, non-securities expertise who are often called upon by their colleagues in the representation of issuers. These non-securities professionals will generally not be in a position to evaluate or even know the facts with sufficient completeness to render a judgment as to whether the aspect of the matter entrusted to them is “material” to the issuer. To subject these non-securities practitioners to the harsh obligations and penalties of the proposed rule is both unfair and counterproductive.

Similarly, the proposed rule creates categories of attorneys denominated as supervisory or subordinate which will substantially compromise the collaborative nature of a law firm or law department practice. We note that this provision seems to assume that lawyers working together are nevertheless definable as supervisors and subordinates, not always the
reality of a particular situation. But no matter what the assumption, if ever there was a provision designed to inhibit the free and open discussion among colleagues, this is certainly one. For example, does the Commission seriously expect that every time a young associate raises an issue with a partner which after discussion and consideration the partner rejects as a concern, the partner will have to document his reasoning and will reject the concern at his peril? Or is it more likely that as a result of this rule, subordinates are going to be increasingly cautious in raising issues with supervisors, thereby depriving the client of fresh and imaginative thinking about a matter? Either way, the losers are the client and the law firm or law department, as well as the public’s concern with assuring the compliance with law by clients will not be enhanced but rather degraded. The attorney in charge the law firm’s practice with regard to a client is the attorney who is practicing and appearing before the Commission. It is impractical for the Commission to attempt to regulate internal practices within a law firm or to ask subordinate attorneys to act independently of the principal attorney in the representation of an issuer.

We therefore suggest that the definition of “representing an issuer” be limited to attorneys employed by or retained by an issuer to act on its behalf as an attorney. We further suggest that the definition of “attorney” be limited to people who are, or hold themselves out to be, admitted, licensed or otherwise qualified to practice law in any domestic jurisdiction. The definition should not include someone who otherwise would fall within the definition but who works on a matter that is before the Commission under the supervision, direction or supervisory authority of another attorney employed by the issuer or the law firm retained by the issuer.

V. THE PROPOSAL TO CREATE A QUALIFIED LEGAL COMPLIANCE COMMITTEE (“QLCC”) SHOULD BE MODIFIED TO REMOVE THE NOISY WITHDRAWAL PROVISION

Paragraph 205.3(c) permits reporting attorneys to follow an alternative reporting procedure and avoid a “noisy withdrawal” if the issuer chooses to establish a committee of at least three non-employee directors (including an audit committee member) with the responsibilities of a “qualified legal compliance committee” described in paragraph 205(2)(j). If the issuer has a QLCC, a reporting attorney has the option of reporting a material violation to the QLCC rather than the chief legal officer. If this alternative procedure is followed, the reporting attorney need not deter-
mine whether the response is appropriate and need not follow the “noisy withdrawal” procedure.

As proposed, a QLCC would have the responsibility of investigating reports, notifying the audit committee or full board of directors, directing the adoption of remedial measures and sanctions to stop the violations and rectify any that have occurred, and informing the chief legal officer and chief executive officer. If the issuer fails to take the remedial measures directed by the QLCC, each member of the QLCC, as well as the chief legal officer and chief executive officer, must also notify the Commission of the material violation and identify any Commission-filed documents that as a result are materially false or misleading.

We believe that the idea behind the QLCC proposal—that a committee of independent directors can be an appropriate and effective mechanism for assessing and dealing with possible material violations—is a sound one. We also believe that the “noisy withdrawal” mechanism reflected in clause (5) of the definition of QLCC substantially reduces the likelihood that issuers will use QLCCs, and, as well, reduces the effectiveness of the QLCC mechanism, because it substantially reduces the likelihood that a QLCC will be able to put difficult issues to rest. To be an attractive option, the QLCC must hold out substantial hope of finality. In particular, the requirement that each member of the QLCC have an independent responsibility to notify the Commission, if the issuer fails “in any material respect” to take directed remedial steps, significantly increases the likelihood of such reporting, even where the committee as a whole is satisfied that problems have been addressed, and further undercuts the QLCC’s usefulness. The “noisy withdrawal” requirement also introduces the same “chilling” effect on attorney-client communications as the other “noisy withdrawal” provisions of the proposed rule discussed elsewhere in this letter. We would therefore eliminate this aspect of the proposed definition.

We believe that many directors will be concerned about the potential heightened risk of liability that may flow from QLCC membership. While this may limit the number of issuers using QLCC’s, it is not, in our view, a reason not to permit use of the QLCC mechanism. However, imposing a “noisy withdrawal” obligation on individual QLCC members can only aggravate this liability concern. For this reason as well, we would eliminate the “noisy withdrawal” requirement.

We also believe the provisions of clause (1) of the definition should be simplified. In particular, we suggest that a QLCC be comprised of any number of non-employee directors designated by the board, which need not include a member of the audit committee, but which alternatively
could consist of the audit committee. As long as the committee members are all non-employees, we do not see any reason to restrict further the board’s flexibility in selecting a suitable membership for the committee. Smaller issuers, in particular, will more likely be able to use the QLCC mechanism if granted this added flexibility.

VI. THE PROPOSAL TO CREATE A QUALIFIED LEGAL COMPLIANCE COMMITTEE ("QLCC") SHOULD BE MODIFIED TO PROVIDE A SAFE HARBOR FOR THE CHIEF LEGAL OFFICER WHO REPORTS UP TO THE QLCC OR AN APPROPRIATE AUDIT COMMITTEE

As noted above, the Commission’s proposed rule regarding the QLCC provides an attorney representing an issuer before the Commission with an effective way to avoid the nettlesome ethical issues that would be presented by a “noisy withdrawal.” This is true whether the attorney is “inside counsel” or “outside counsel.” No such safe harbor, however, is provided to the issuer’s Chief Legal Officer. The Commission’s proposed rule provides that even where a CLO avails himself or herself of the alternative method of reporting a violation provided by 205.3(c), he or she is still responsible for reporting that violation to the Commission should the issuer not take appropriate remedial action after the QLCC finishes its investigation and makes its recommendation. We believe that the very same ethical concerns presented by the “noisy withdrawal” provisions to outside counsel for the issuer as well as inside counsel apply equally to the CLO as the issuer’s chief attorney. Accordingly, we believe it would be appropriate to afford the CLO the same “safe harbor” that the Commission has provided to the rest of the issuer’s attorneys. The Commission should revise its proposed rule to make it clear that where a CLO reports a material violation to a QLCC, he or she “is not required to assess the issuer’s response to the reported evidence of a material violation, and is not required to take any action under paragraph (d) of this section regarding the evidence of a material violation.”

VII. THE SANCTION FOR VIOLATION OF THE PROPOSED RULE SHOULD BE LIMITED TO DISCIPLINARY PROCEEDINGS UNDER RULE 102(E)

Another area of great concern to the CityBar, is the Commission’s attempt to assume the power to bring an enforcement action against attorneys for violating the proposed rule. As discussed below, we believe
that the sanction for violating the rules of conduct promulgated by the
Commission pursuant to Section 307 of the Act should be limited to dis-

The very first paragraph of the proposed rule states:

A violation of this part by any attorney appearing and practic-
ing before the Commission in the representation of an issuer
shall be treated for all purposes in the same manner as a viola-
seq.), and any such attorney shall be subject to the same penal-
ties and remedies, and to the same extent, as of a violation of
that Act

The Commission relies upon Section 3 (b) of the Act to justify this
extreme position. Section 3(b) of the Act provides:

A violation by any person of this Act, any rule or regulation of
the Commission issued under this Act, or any rule of the Board
shall be treated for all purposes in the same manner as a viola-
seq.) or the rules and regulations issued thereunder, consistent
with the provisions of this Act, and any such person shall be sub-
ject to the same penalties, and to the same extent, as for a vio-
lation of that Act or such rules or regulations. (emphasis added.)

As noted below, however, it is far from clear whether Congress intended
to subject attorneys to an enforcement action brought by the Commis-
sion for failure to comply with the rules of conduct promulgated pursu-
ant to Sec. 307.

Section 307 of the Act directs the Commission to “issue rules, in the
public interest and for the protection of investors, setting forth mini-
mum standards of professional conduct for attorneys appearing and prac-
ticing before the Commission.” (emphasis added). Section 4C of the Exchange
before the Commission. That section provides simply that the Commis-
sion may censure any person who, after notice and opportunity to be
heard, is found to be lacking in competence or integrity or who is found
to have willfully aided and abetted a violation of the securities laws. That
section does not provide that a violation of the Commission’s rules of
conduct constitute a substantive violation of the Exchange Act, nor does
that section give the Commission the ability to bring an enforcement
action for a violation of its rules of conduct. If Congress had intended to
empower the Commission to bring such enforcement actions, we believe
it is self-evident that Congress would expressly have amended this section
to so provide.

Equally troubling is the Commission’s attempt to incorporate in its
proposed rules the definition of “improper professional conduct” con-
tained in Section 602 of the Act. The definition of “improper professional
conduct” set forth in the Act by its express terms does not apply to attor-
neys.

Proposed Section 205.6(b), which seeks to define “improper profes-
sional conduct,” provides:

With respect to attorneys appearing and practicing before the
Commission on behalf of an issuer, “improper professional con-
duct” under section 4C(a) of the Securities Exchange Act of 1934
(15 U.S.C. 78d-3(a)) includes:

(1) Intentional or knowing conduct, including reckless conduct,
that results in a violation of any provision of this part; and

(2) Negligent conduct in the form of:

(i) A single instance of highly unreasonable conduct that
results in a violation of any provision of this part; or

(ii) Repeated instances of unreasonable conduct, each result-
ing in a violation of a provision of this part.

In the release seeking comments on the proposed rule, the Commission
states that Congress, in enacting Section 602 of the Act, “amend[ed] the
Exchange Act to add Section 4C(a), which incorporates that portion of
the text of Rule 102(e) providing the Commission with the authority to
discipline professionals for improper professional conduct.” The Com-
mission then concludes that this provision applies to attorneys and states:
“Accordingly, an attorney who violates any provision of Part 205 engages
in improper professional conduct.” However, the Commission’s conclu-
sion is contradicted the express language of the Act.

The definition of “improper professional conduct” in Section 602 of
the Act is expressly limited to “registered public accounting firms.” The
term “registered public accounting firms” is defined in the Act as referring
to public accounting firms that are registered with the Commission. By
its express terms, the definition of “improper professional conduct” in
Section 602 does not apply to attorneys.
Nor does any language in the rest of the Act to suggest that Congress intended to subject attorneys to enforcement actions for violations of the “minimum standards of professional conduct” called for by Section 307 of the Act.

A. The Commission Should Include Language In The Regulation That Makes Clear That A Violation Of The Regulation Does Not Expose The Attorney To Criminal Liability

In its Release, when discussing proposed rule 205.6, the Commission states that “The Commission does not believe, however, that violations of the proposed rule would, without more, meet the standard prescribed in Section 32(a) of the Exchange Act (15 U.S.C. 78ff), which provides for the imposition of criminal penalties.” As discussed above, we believe that proposed rule 205.6 should be revised to limit the sanctions for violating the regulations to disciplinary proceedings pursuant to Rule 102(e). We do not believe that Congress intended, nor do we believe that the language of the Act provides, that a violation of the rules of conduct promulgated by the Commission pursuant to Section 307 should rise to the level of a violation of the Exchange Act. Therefore, we believe that the Commission when revising proposed rule 205.6 should make it clear that a violation of the rules promulgated pursuant to Section 307 cannot and shall not subject an attorney to criminal penalties.

B. The Commission Should Clarify That Attorneys Subject To The Proposed Rule Owe A Duty Solely To Their Client, The Corporate Entity, And Not To Investors, And Should Modify The Language In The Proposed Rules To Clarify That There Is No Private Right Of Action For Violation Of The Proposed Rule

Section 205.3(a) of the proposed rule states that:

An attorney appearing and practicing before the Commission in the representation of an issuer represents the issuer as an organization and shall act in the best interest of the issuer and its shareholder . . .

This statement mischaracterizes the relationship between legal counsel to an issuer and the issuer, and incorrectly states that that issuer’s counsel has a duty to the shareholders.

The Model Rules and New York Code identify many duties running from attorneys to their clients, including duties of loyalty, confidential-
ity and competence.\footnote{See Model Rules of Professional Conduct, Rules 1.7 (duty of loyalty requires absolute fidelity by the attorney to the client); Rule 1.6 (duty of confidentiality requires attorney to maintain inviolate the client’s confidential information); and Rule 1.1 duty of competence requires attorneys to act with requisite knowledge, skill, thoroughness and preparation); see also NY Code, DR, 4-101 (Lawyer shall not knowingly reveal a client confidence or secret); DR NY Code DR 6-101 (Lawyer shall not handle a legal matter which the lawyer knows or should know he or she is not competent to handle or is without adequate preparation, and shall not neglect a legal matter entrusted to the lawyer).} The only instance in which a lawyer is charged with acting in the “best interest” of an organization occurs when the lawyer knows that (1) an individual associated with the organization is violating a legal duty; and (2) the behavior is likely to result in substantial injury to the organization. Only in this narrow circumstance is a lawyer charged with proceeding “as is reasonably necessary in the best interest of the organization,” which may include up-the-ladder reporting.\footnote{Model Rules, Rule 1.13; NY Code, DR 5-109.} On the contrary, officers and directors are charged with determining the company’s best interests, and are protected from undue exposure to liability by the business judgment rule.\footnote{Restatement (Third) of the Law Governing Lawyers § 96 cmt. F (2000). Under the “business judgment rule,” officers and directors are not liable for errors or mistakes in judgment so long as they were disinterested and independent, acted in good faith, and were reasonably diligent in keeping informed of the relevant facts.} Thus, while issuer’s counsel is obligated to provide competent legal advice, it is up to management to select the course of action that is in the best interest of the corporation in light of all relevant considerations, including legal advice obtained from counsel. The Commission’s proposed imposition on attorneys of a duty to act in the best interest of their corporate clients unreasonably increases counsel’s exposure to lawsuits by private litigants, who will use this language to charge that attorneys failed to intervene in the company’s “best interest.”

In addition, under both the Model Rules and the New York Code, a lawyer who is employed or retained to represent an organization as a client represents only the organization, and not the constituents of the organization—a group that would include officers, directors, employees, members and shareholders.\footnote{Model Rule 1.13(a); NY Code, DR. 5-109(a).} The principle that the company counsel’s duty of loyalty and competence runs solely to the organization has been confirmed repeatedly in federal and state courts.\footnote{See, e.g., Pellettier v. Zweifel, 921 F.2d 1465 (11th Cir.), cert. denied, 502 U.S. 855 (1991) (shareholder may not sue entity’s lawyer for violation of duties to shareholder because lawyer’s fiduciary duty is to the entity); Egan v. McNamara, 467 A.2d 733 (D.C. 1983) (lawyer...
organization’s interests become adverse to those of a constituent, the lawyer must advise the constituent that he or she cannot represent such constituent. Accordingly, the proposed rule’s statement that lawyer’s must act in the best interest of shareholders is plainly contradicted by the Model Rules, the New York Code, and case law, and therefore the rule should be revised. We suggest that Section 205.3(a) be revised to state that “[a]n attorney appearing and practicing before the Commission in the representation of an issuer represents the issuer and owes his or her professional and ethical duties to the issuer.”

Moreover, the suggestion in the language of the proposed rule that the attorney for the issuer also owes a duty to the shareholders contradicts the view expressed by the Commission in the release that “nothing in Section 307 creates a private right of action against an attorney.” The statement that the attorney must act in the best interest of the issuer’s shareholders suggests that a failure to do so could form the basis for a private action against the attorney by any of these shareholders.

During the debate in the Senate on amendment to Sarbanes-Oxley, which ultimately became §307, Senator Edwards, one of the sponsors of the amendment, noted:

Nothing in this bill gives anybody a right to file a private lawsuit against anybody. The only people who can enforce this amendment are the people at the SEC. They will enforce this amendment not on behalf of any private party, but in the name of the American people....

Similarly, Senator Enzi, a co-sponsor of the amendment, noted in his statement in support:

“... this amendment creates a duty of professional conduct and does not create a right of action by third parties.” (Emphasis added)

Like the legislation itself, the Commission’s proposed rules are silent with respect to creating a private right of action. The question arises, however, whether absent an express disclaimer, there is a risk that courts might imply a private right of action from the creation of a new Commission Rule which imposes new obligations on attorneys.


The principal vehicle by which private actions are brought pursuant to the securities laws is, of course, 10(b)(5) promulgated pursuant to 15 U.S.C. §78(j) (§10[b] of the Securities Exchange Act of 1934). The courts have long implied a private right of action for violations of 10(b)(5). However, the courts have also limited the class of potential defendants to persons who have directly engaged in conduct violative of the rule, i.e. persons who have engaged in a device, scheme or artifice to defraud, or who have deliberately made untrue statements of a material fact or material admissions, or have engaged in acts or practices operating as a fraud. The Supreme Court has held that individuals who have merely aided and abetted violations of 10(b)(5) are not subject to a private lawsuit. Central Bank of Denver, N.A. the First Interstate Bank of Denver, N.A., 511 U.S. 164 (1994). Similarly, auditors for issuers have been held not to be liable to private parties (other than the issuer) for negligence in the preparation of audited financial statements. Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976).

Even prior to Central Bank, which abolished aiding and abetting liability in private actions, plaintiff’s have found it difficult to survive motions to dismiss 10(b)(5) actions against law firms representing issuers. See generally Towers Financial Corporation Securities Litigation, 1995 U.S. Dist. Lexis 21147, at p. 44, fn. 13 (SDNY 1995 (report of Andrew J. Peck, United States Magistrate))(report adopted at 1996 U.S. Dist. Lexis 11008 (SDNY 1996)), which contains a compendium of Second Circuit and Southern District of New York cases in which claims against lawyers have been dismissed.

Most cases seeking to impose liability on attorneys founder for failure adequately to allege privity or one or more of the requisites for proof in a private securities fraud litigation, including reliance, causation, absence of a purchase or sale, or scienter. Several cases note that there is no direct duty between a corporation’s attorneys and its shareholders, or investors.

Notwithstanding the substantial body of case law in which claims against issuers’ attorneys have been dismissed, the reference to a duty owed by issuer’s counsel to the issuer’s shareholders in Section 205.3(a), while probably not intended to create a new duty for issuer’s counsel directly to shareholders, still creates the risk that the language may be interpreted by some to satisfy the requirement of privity.

Additionally, §205.6(a) provides that

A violation of this part by any attorney appearing and practicing before the Commission in the representation of an issuer shall be treated for all purposes in the same manner as a viola-
tion of the Securities Exchange Act of 1934 (15 U.S.C. 78(a) et seq.) and any such attorney shall be subject to the same penalties and remedies, and to the same extent, as for a violation of that Act.” (Emphasis supplied)

While it is doubtful that, in the context of the rule, the Commission meant to imply that an attorney is subject to a private right of action as if he had violated §10(b)(5) or one of the other sections of the act giving rise to private rights of action, the language of §205.6(a) creates the potential for confusion. Reading these two sections of the Rule together, a private litigant might claim that private right of action exists on behalf of shareholders who purchase or sell an issuer’s securities where, for example, an attorney is later found by the Commission to have uncovered “evidence” of a violation of the rules, but failed to comply with disclosure requirements. Indeed, some might read this section (which imposes sanctions on attorneys for negligent conduct, §205.6[b][2]) as creating a new duty on the part of attorneys to shareholders (as distinct from the issuer) and a new ground for imposing civil liability.

Accordingly, we believe the Commission should modify proposed Part 205 to remove any reference to a duty to act on behalf of shareholders, and amend the regulation to include a “safe harbor” provision to clarify that no private right of action against the attorney is created by the rules of conduct being promulgated by the Commission pursuant to Section 307 of the Act.

C. The Commission Should Add A Safe Harbor Provision Regarding Shareholder Suits

There is no “safe harbor provision” in the Act protecting attorneys from private actions brought by shareholders. Congress enacted Section 10A(3)(c) of the Exchange Act to provide a “safe harbor” provision protecting auditors from private causes of action for failure to comply with the “up the ladder” reporting requirements. Section 10A(3)(c) of the Exchange Act provides:

(c) Auditor liability limitation. No registered public accounting firm shall be liable in a private action for any finding, conclusion, or statement expressed in a report made pursuant to paragraph (3) or (4) of subsection (b), including any rule promulgated pursuant thereto.

Yet, no such provision protecting attorneys is explicitly included within
the Act. Thus, one could argue that since Congress demonstrated its ability to protect auditors from private suits for failure to comply with the “up the ladder” reporting requirements, its decision not to provide similar protection to attorneys must have been deliberate.

We do not believe that Congress did not include attorneys within the statutory safe-harbor provision because it intended to expose attorneys to shareholder actions. The floor debate, as described earlier, makes it clear Congress did not wish to create that kind of liability. We believe Congress never anticipated that the Commission would promulgate regulations that were so broad that they would carry the potential of creating attorney civil liability. Therefore, a statutory safe-harbor was not needed.

The Commission should, at a minimum, include a provision in its rule protecting attorneys from potential unintended consequences of the rules’ breadth. If it is not the Commission’s intent to expose attorneys to private liability for failure to adhere to the new rules, it should say so.

D. The Definition of Appearing And Practicing Before The Commission Should Not Include Advice That A Party Is Not Obligated To Submit Or File A Registration Statement

Section 307 of the Act directs the Commission to issue rules setting forth minimum standards of professional conduct for attorneys appearing and practicing before the Commission. Section 2.05.2(a)(5) (ii) of the Proposed Rule provides that appearing and practicing before the commission includes “Advising a party that “(ii) The party is not obligated to submit or file a registration statement, notification, application, report, communication or other document with the Commission or its staff.”

The language quoted above is a significant expansion of what would commonly be understood to constitute appearing and practicing before the Commission. Over the past decades, the Commission has adopted a series of Rules designed to simplify the process of raising money in a variety of “private placement” transaction in order to avoid delays and costs entailed in registering securities with the Commission. By and large, these rules have been effective in accomplishing their objectives without giving rise to systemic problems involving fraud or evasion of the securities laws. A number of years after adoption of Regulation D, for example, the Commission conducted a nation-wide review of numerous transactions claiming the exemption under Regulation D for the purpose of determining whether that safe harbor was being used to perpetuate fraud. Such review did not identify serious issues warranting restricting the use of safe harbor.

The recent events giving rise to the adoption of the Act did not in-
volve non-reporting companies and nothing suggests that the Commission intended to impose the Act's regimen on non-reporting companies. The financial resources of many of these companies are limited and to subject such companies to the scope of the new Commission rules is unwarranted by any perceived deficiencies in the existing regulatory scheme and uncalled for by the Act. In light of the above, to create a new and expansive definition of practicing before the Commission, which would then bootstrap a dramatic range of new procedures applicable to reporting companies and apply these procedures to non-reporting companies, seems to be an unwarranted expansion of the Commission’s activities well beyond the intention of the Act.

Taken to its extreme, and in light of the proposed rule’s ambiguities, attorneys rendering advice to non-reporting companies regarding private placements would now be required to report to the Commission any violation of securities laws or breaches of fiduciary duty by non-public companies. The Act does not attempt to apply the wide-range of enacted corporate governance provisions to these private companies, and it is hard to imagine that it was the intent of Congress in passing the Act to broaden the Commission’s activities in the non-public company context.

Attorneys play a major role in aiding non-reporting companies in conducting private placements in a manner which undoubtedly raises the compliance levels of these financial activities to a significant extent. To turn outside counsel of these companies into an enforcement arm of the Commission as a condition to obtain legal advice regarding compliance with private placement rules would likely reduce the role of attorneys in these areas and therefore adversely affect overall compliance with securities laws.

E. The Definition of “Fiduciary Duty”

Section 307 of the Act requires the Commission to issue rules regarding standards for practice before the Committee, including a rule requiring an attorney to provide evidence of breach of fiduciary duty22 (or similar material violations by the company).23 Proposed Rule 205.2(d) defines

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22. The language of Section 307 of the Act is ambiguous as to whether the “material” qualifier modifies breach of fiduciary duties or only violations of securities laws. We agree with the Commission’s clarification—applying the modifier to all violations and breaches. Congress did not intend to extend the new rule to minor violations.

23. The issue of what is meant by a “similar material violation” is beyond the scope of this comment. Additional time should be permitted by the Commission to allow for comment on this and numerous other issues that could not be addressed herein.
“breach of fiduciary duty” as follows: “(d) Breach of fiduciary duty refers to any breach of fiduciary duty recognized at common law, including, but not limited to misfeasance, nonfeasance, abdication of duty, abuse of trust, and approval of unlawful transactions.” The explanatory material indicates that definition is intended to identify typical common law breaches of fiduciary duty.

Issues involving fiduciary duty are governed by state law and vary from state to state. There is no federal law of fiduciary duty. Issues involving alleged breaches of fiduciary duty have generally been resolved through civil litigation and not by means of intervention of the Commission. While certain aspects of fiduciary duty are related to securities laws, such as breaches of fiduciary duty which involve fraud and possibly those involving self-dealing, a whole array of potential fiduciary violations and have nothing to do with securities laws and should not be subject to expanded activities by the Commission. Expanding the reach of the Commission’s authority and the application of the federal securities laws to all aspects of fiduciary duties is a dramatic change in the legal system’s approach to the issue of fiduciary duty. Such a dramatic change is unwarranted by any of the events leading up to the Act.

Finally, we believe it is unrealistic to require an attorney for an issuer to be fully conversant in the common law of all 50 states (plus Puerto Rico) in the area of fiduciary duty. Accordingly, we recommend that the definition of breach of fiduciary duty as defined in Proposed Part 205 be limited to breach of fiduciary duty as defined in the common law of the issuer’s state of incorporation.

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Professional Discipline
Securities Regulation
Professional & Judicial Ethics
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Professional Discipline
Professional & Judicial Ethics
Professional Discipline
Professional Responsibility
Corporation Law
Part 205—Standards of Professional Conduct for Attorneys
Appearing and Practicing Before the Commission in the
Representation of an Issuer

[Index to Rule]

(3) Purpose and scope
Consistent with Section 307 of the Sarbanes-Oxley Act of 2002, 15 U.S.C. 7245, the Commission is adopting rules setting forth the minimum standards of professional conduct for attorneys appearing and practicing before it in the representation of an issuer. The rules may be used, pursuant to Part 102, to censure, suspend or bar an attorney from appearing or practicing before the Commission. A violation of the rules, regardless of the mental culpability of the actor, is not a criminal act as defined by 15 U.S.C. ‘78ff. The Rules are not intended to create a private right of action for any person against the actor.

(4) Definitions
For purposes of this part, the following definitions apply:

a. Appearing and practicing before the Commission shall have the meaning in Rule 102(f) and includes, but is not limited to:
   i. Transacting any business with the Commission, including with Commissioners, the Commission, or its staff;
   ii. Representing any party to, or the subject of, or a witness in a Commission administrative proceeding;
   iii. Representing any person in connection with any Commission investigation, inquiry, information request, or subpoena; and
   iv. Preparing or participating in the preparation of any registration statement, periodic report or other writing with to be filed with, or is to be incorporated by reference into any document that is filed with, the Commission or its staff (but excluding preparing or participating in the preparation of a writing that is not intended to be filed with or submitted to the Commission or its staff or is not intended to be incorporated by reference into any document that will be filed with the Commission but is used in connection with any such filing or submission).

b. Appropriate response means a response to evidence of a material
violation reported to appropriate officers or directors of an issuer as provided by these rules that provides a basis for an attorney who has reported such evidence to believe, in good faith:

i. That no material violation is occurring or is about to occur; or

ii. That the issuer has adopted measures that can be expected to stop any material violation that is occurring, and/or prevent any material violation that has yet to occur.

c. Attorney means any person who is, or holds himself or herself out as, admitted, licensed, or otherwise qualified to practice law in any domestic jurisdiction but shall not include an attorney who works under the supervision, direction or supervisory authority of another attorney employed by the issuer or the firm retained by the issuer with regard to the matter in question.

d. Breach of fiduciary duty means the breach of any fiduciary duty recognized at common law of the jurisdiction of incorporation.

e. Evidence of a material violation means information that an attorney knows which clearly establishes that a material violation has occurred, is occurring or is about to occur.24

f. In the representation of an issuer means being employed or retained by the issuer to act on its behalf as an attorney.

g. Issuer means an issuer (as defined in Section 3 of the Securities Exchange Act of 1934 (15 U.S.C. 78c)), the securities of which are registered under Section 12 of that Act (15 U.S.C. 78l), or that is required to file reports under Section 15(d) of that Act (15 U.S.C. 780(d)), or that files a registration statement that has not yet become effective under the Securities Act of 1933 (15 U.S.C. 77a et seq.), and that it has not withdrawn.

h. Material violation means a violation of the securities laws, breach of fiduciary duty, or similar violation which in each case is a violation of a legal obligation to the organization, or a violation of law that reasonably might be imputed to the organization and is likely to result in substantial injury to the organization.25

i. Report means to make known to directly, either in person, by telephone, by email, electronically, or in writing.

(5) Issuer as client

a. An attorney appearing and practicing before the Commission in the representation of an issuer represents the issuer as an organiza-
tion. That the attorney may work with and advise the issuer’s officers, directors or employees in the course of representing the issuer does not make such individuals, or its shareholders, the attorney’s clients. When it appears that the organization’s interest may differ from those of the constituents with whom the lawyer is dealing, the lawyer shall explain that the lawyer is the lawyer for the organization and not for any of its constituents.26

(6) In the representation of an issuer a lawyer shall not:
   a. engage in conduct involving dishonesty, fraud, deceit, or misrepresentation;27
   b. conceal or knowingly fail to disclose that which the lawyer is required by law to reveal;28
   c. knowingly make a false statement of law or fact;29
   d. counsel or assist the client in conduct that the lawyer knows to be illegal or fraudulent;30 or
   e. knowingly engage in other illegal conduct or conduct contrary to a rule contained within this Part 205.31

(7) Duty to Report Evidence of Material Violation
   a. Duty to report evidence of a material violation.
   ii. Subject to the provisions of subparagraph (iv), if, in appearing and practicing before the Commission in the representation of an issuer, an attorney knows of evidence of a material violation by the issuer or by any officer, director, employee or agent of the issuer acting in such capacity, the attorney shall report such evidence to the issuer’s chief legal office (or the equivalent thereof) or to both the issuer’s chief legal officer and its chief executive officer (or to the equivalent thereof) forthwith.
   ii. Subject to the provisions of subparagraph (iv), the chief legal officer (or the equivalent thereof) shall cause such inquiry into the evidence of a material violation as he or she believes is necessary to determine whether the material violation as described in the report is occurring, or is about to occur. If the chief legal officer believes that no material violation is occurring, or is

26. DR 5-109(A)
27. DR 1-102(A) (4)
28. DR 7-102 (A) (3)
29. DR 7-102 (A) (5)
30. DR 7-102 (A) (7)
31. DR 7-102 (A) (8)
about to occur, he or she shall so advise the reporting attorney. If the chief legal officer believes that a material violation is occurring, or is about to occur, he or she shall proceed to seek to ensure that the issuer adopts appropriate measures to stop any material violation that is occurring, or to prevent any material violation that is about to occur. The chief legal officer shall promptly report the measures adopted to the chief executive officer, to the audit committee of the issuer's board of directors, or to the issuer's board of directors, and to the reporting attorney.

iii. If an attorney who has made a report under paragraph (b) does not receive an appropriate response to his or her report, the attorney shall report the evidence to the audit committee of the board of directors of the issuer or to another committee of the board of directors comprised solely of directors not employed directly or indirectly by the issuer, or to the board of directors.

iv. A lawyer acting pursuant to this paragraph shall proceed as is reasonably necessary in the best interest of the organization. In determining how to proceed, the lawyer shall give due consideration to the seriousness of the violation and its consequences, the scope and nature of the lawyer's representation, the responsibility in the organization and the apparent motivation of the person involved, the policies of the organization concerning such matters and any other relevant considerations. Any measures taken shall be designed to minimize disruption of the organization and the risk of revealing information relating to the representation to persons outside the organization. Provided:

(a) A lawyer may reveal confidences or secrets to the extent implicit in withdrawing a written or oral opinion or representation previously given by the lawyer and believed by the lawyer still to be relied upon by a third person where the lawyer has discovered that the opinion or representation was based on materially inaccurate information or is being used to further a crime or fraud32; and

(b) A lawyer may reveal the intention of a client to commit a crime and the information necessary to prevent the crime.33

(8) Withdrawal from Representation

a. Where an attorney who has reported evidence of a material viola-

32. DR 4-101 (C)(5)
33. DR 4-101 (C)(3)
tion under Section 205.4 hereof does not receive an appropriate response, or has not received a response in a reasonable time, to his or her report, and the attorney believes that a material violation is ongoing or is about to occur:

i. An attorney employed by a law firm retained by the issuer shall withdraw forthwith from representing the issuer, and report to the audit committee and the board of directors that the withdrawal is based on professional considerations; and

ii. An attorney employed by the issuer shall disassociate himself or herself from such material violation, and report to the audit committee and the board of directors of his or her disassociation and that his or her disassociation is based on professional considerations.
Taking Aim:
New York State’s
Regulation of Firearms
and Proposals for Reform

The Committee on State Affairs

Like the Second Amendment to the U.S. Constitution, Section 4 of the New York Civil Rights Law provides that, “[a] well regulated militia being necessary to the security of a free state, the right of the people to keep and bear arms cannot be infringed.” The provision is interpreted, however, to “protect only the right to be armed with weaponry suitable for use by the militia in warfare and for the general defense of the community.” Possession of a firearm in New York, therefore, is a privilege subject to reasonable regulation.

This report provides an overview of existing firearms regulation in New York, and thereby identifies four specific areas in need of improved or additional regulation. These proposed reforms will make legally-owned firearms safer and will limit the proliferation of illegal firearms. The four areas are:

1. U.S. Const. amend. II; N.Y. Civil Rights Law § 4 (McKinney 1992). The Second Amendment itself “is a limitation only upon the power of Congress and the National government, and not upon that of the States,” and therefore does not apply to state legislation. Presser v. Illinois, 6 S. Ct. 580, 584 (1886); see also Malloy v. Hogan, 84 S. Ct. 1489, 1491 n.2 (1964); Citizens for a Safer Comm. v. Rochester, 627 N.Y.S.2d 193, 197 (Sup. Ct. 1994).


4. A discussion of the criminal sentences provided by New York law for crimes that involve
STATE AFFAIRS

- Licensing reform, primarily to improve enforcement of existing rules and regulations;
- Additional forms of protection against improper gun ownership and misuse, including safe storage rules, one-gun-a-month limits, ammunition controls, ballistic fingerprinting for long guns, and increased restrictions on specific weapons categories;
- Expanded civil liability for illegal sellers and manufacturers of firearms; and
- Enhanced interdiction programs to combat the illegal influx of guns from other states.

The following sections explore how each of these proposals would improve existing regulation.

I. PROPOSALS FOR STRENGTHENING NEW YORK’S LICENSING REGIME
A. The Current Licensing System
Possession of a “firearm” in New York requires a license, pursuant to Section 400 of the Penal Code. However, “firearms” are defined to include only: pistols and revolvers; shotguns with barrels less than eighteen inches in length; rifles with one or more barrels less than sixteen inches in length; any weapon made from a shotgun or rifle by alteration or modification; and, beginning in 2000, assault weapons. Rifles and shotguns that do not fall within this definition are known as “long guns” and, except in New York City, require no license.

To hold a firearms license, an applicant must be twenty-one years of age and of good moral character. In addition, an applicant cannot have been convicted of a felony or other serious offense, and must not be disqualified by mental illness or by a court pursuant to an order of protection. Fur-

5. N.Y. Penal Law § 400.00(2) (McKinney 2000).
6. Id. § 265.00(3).
7. Localities may promulgate regulations on the public storage, possession, and display of firearms, ammunition, and explosives. However, these local regulations may “not apply to the personal possession, use or ownership of firearms or ammunition therefor.” N.Y. Gen. Mun. Law § 139-d (McKinney 1999); N.Y. Town Law § 130(5) (McKinney 1987).
8. N.Y. Penal Law § 400.00(1). On the issuance or violation of a temporary or final order of protection, a court may suspend the defendant’s firearms license, order him ineligible for a
ther, there must be no “good cause” for the denial of a license.\textsuperscript{9} The applicant also must provide a photograph, fingerprints, and physical descriptive data to local law enforcement authorities to enable the State’s Division of Criminal Justice Services in Albany and the Federal Bureau of Investigation to determine whether he or she has a criminal record.\textsuperscript{10}

The State must issue or deny the application within six months of filing.\textsuperscript{11} The successful applicant, whose name thereby becomes public record, may then receive a license for a pistol or revolver, but not an assault weapon or disguised gun.\textsuperscript{12}

The basic license permits the holder to keep a gun in his or her home or place of business.\textsuperscript{13} However, a licensed firearm may not be willfully discharged in a public place, or aimed or fired at another person unless in self-defense or in the discharge of official duty.\textsuperscript{14} To obtain a broader license to carry a concealed weapon, the applicant must show proper cause

\textsuperscript{9} N.Y. Penal Law \$ 400.00(1). Examples of “good cause” include public safety concerns, misrepresentations on the application, and sexual misconduct. See, e.g., Nash v. Police Dep’t of the City of New York, 708 N.Y.S.2d 61 (1st Dep’t 2000); Harris v. Codd, 394 N.Y.S.2d 210 (1st Dep’t 1977).

\textsuperscript{10} N.Y. Penal Law \$\$ 400.00(3), (4). Non-discrimination provisions do not bar inquiry into prior arrests and convictions. N.Y. Exec. Law \$ 296(16) (McKinney 2000).

\textsuperscript{11} N.Y. Penal Law \$ 400.00(4-a).

\textsuperscript{12} Id. \$\$ 400.00(5), (2).

\textsuperscript{13} Licensees may also use pistols and revolvers at pistol and shooting ranges, or as part of a university pistol team. Id. \$ 265.20(7), (12). Nonresidents may travel into the State with unlicensed pistols and revolvers to competitive pistol matches or competitions, organized conventions, and exhibitions, provided that the guns are transported unloaded in locked, opaque containers with documentation about the event. Id. \$ 265.20 (13).

\textsuperscript{14} Id. \$ 265.35. Special provisions have been made for peace officers, security guards, and the militia. Pursuant to training and licensing requirements, peace officers are empowered to possess and take custody of firearms. N.Y. Crim. Proc. Law \$ 2.20. Security and armored car guards are entitled to use their weapons for the protection of others. N.Y. Gen. Bus. \$ 89-L – n (McKinney 1998). Members of the state militia have the exclusive right to parade with firearms. N.Y. Mil. LAW \$ 170 (McKinney 1990).

Regardless of licensing, possession or display of a pistol, revolver, rifle, shotgun, machine gun or other firearm during the commission of a violent felony is an “armed felony.” N.Y. Penal Law \$ 265.08, .09. Similarly, criminal use of a firearm in the first degree carries an enhanced sentence of five additional years. Id. \$ 265.09(2). Sentences are also enhanced for commission of certain general crimes with a firearm, including: menacing, id. \$ 120.14; criminal trespass, id. \$ 140.17; grand larceny, id. \$ 155.30; and criminal contempt, id. \$ 215.51.
for the license, meaning “a special need for self-protection distinguishable from that of the general community or of persons engaged in the same profession.”

Licenses are non-transferable and are generally valid throughout the state. In New York City, they must be renewed every three years, and in Nassau, Suffolk, and Westchester counties, every five years. Throughout the rest of the state, however, gun owners are not required to renew their licenses, and licenses to carry or possess are valid for life.

When delivering a firearm or ammunition, a seller must require the buyer to produce a license. The licensed buyer must register each firearm with local law enforcement authorities upon purchase. The authorities then record the new firearm on the buyer’s license, and send the purchase record and a copy of the amended license to the New York State Police’s Pistol Permit Bureau. The Bureau records these transactions in a statewide database in an effort to track the ownership status of all legally-owned firearms in the State.

Possession of a firearm without a license is punished under Section 265 of the New York Penal Law. It is illegal to dispose of any weapon without a license. In 2000, the New York Penal Law was amended to prevent any person who is prohibited by law from possessing a firearm, rifle, or shotgun from attempting to purchase one. More importantly, the amendments outlawed straw purchases, whereby one person, who is legally entitled to possess a weapon, purchases a weapon for another who is not. All sales at gun shows were also made contingent upon a national criminal background check.

The 2000 amendments to the New York Penal Law also clarified the State’s assault weapons law. Tracking federal legislation, state law now defines “firearms” to include assault weapons. Assault weapons thereby became the subject of already existing laws prohibiting the possession,

16. N.Y. Penal Law § 265.17(10).
17. Id. § 400.00(12); Id. § 270.00(5).
18. See http://www.troopers.state.ny.us/Firearms/Firearmsindex.html.
19. N.Y. Penal Law § 265.10(7). It is also criminal knowingly to buy, receive, dispose of, or conceal a weapon that has been defaced for the purpose of concealment, prevention of the detection of a crime, or misrepresentation of the identity of the weapon. Id. § 265.10(3).
20. Id. § 265.17.
21. Id. §§ 896(1), 897(1).
22. Id. § 265.00(3)(e).
use, and sale of firearms. At the same time, certain assault weapons, such as semiautomatic rifles, shotguns, and pistols, and a number of specifically delineated weapons, including TEC-9s and Uzis, are banned outright. However, outside of New York City, if such weapons were lawfully possessed prior to September 14, 1994, they are not defined as assault weapons, and are subject to the relevant licensing provisions for firearms.

B. Proposals to Improve the Licensing System
The State’s licensing system suffers from three shortcomings that limit its effectiveness in keeping guns out of the hands of ineligible purchasers.

1. Improving License Renewal Requirements
To ensure that newly-ineligible purchasers do not possess firearms, the law should be changed to require every license to be renewed every three years. This renewal requirement will also enable law enforcement to verify that licensees have properly registered the guns in their possession and have properly recorded all secondary sales. Further, it will help ensure that the database of firearm owners kept by the State Police includes updated information, and thus improve the tracking of firearms used in crimes.

Similar reforms have been implemented outside New York. For example, California recently established a renewal requirement that allows law enforcement authorities to compare the records of handgun buyers going back to 1991 with criminal and other records to identify handgun owners who are no longer allowed to possess their weapons.

2. Licensing Rifles, Shotguns, and Other Long Guns
The Centers for Disease Control and Prevention’s Firearm Injury Surveillance Study estimates that from 1993 to 1997 shotguns or rifles inflicted 18% of nonfatal gunshot wounds in the United States. The FBI’s Supplemental Homicide Reports estimate that during the same period the same kind of weapons were responsible for approximately 11% of all ho-

23. Finally, the legislation amended a number of crimes to specifically include assault weapons and large capacity ammunition feeding devices. § 265.02(7), (B).
24. § 265.00(22) (a), (c), (d).
25. § 265.00(22) (e) (v). The exception tracks federal law.
micides. Moreover, according to the federal Bureau of Alcohol, Tobacco and Firearms’ (“ATF”) 1999 Crime Gun Trace Report, shotguns and rifles comprised 21% of all crime guns traced by law enforcement. Twelve percent of all crime gun trace requests involved two types of long gun, the 12-gauge shotgun and the .22 caliber rifle, which together accounted for more than 57% of all long gun trace requests. Yet, as noted, outside of New York City, there is no license required to possess or purchase a long gun.

Undeniably, handguns are used much more often than long guns in the commission of crimes. But the findings above show that the criminal use of long guns is too significant to exempt such weapons from the State’s licensing regime entirely. Rifles pose a particular threat to law enforcement officers because a rifle bullet travels much faster, and will therefore pierce body armor more easily, than a bullet fired from a handgun.

The local regulation of rifles and shotguns in New York City provides a workable model for statewide statutory reform. Section 10-303 of New York City’s Administrative Code mandates that a permit is required for possession and purchase of rifles and shotguns. To be eligible for a permit in New York City, an applicant must affirm that he or she meets certain eligibility requirements, and provide a recent photograph, fingerprints, physical description, name, occupation, residence, date of birth, and a fifty-five dollar application fee. The New York City Police Department must investigate each application, including a criminal background check on every applicant. New York City rifle and shotgun permits are non-transferable and are valid for three years. They can be automatically

27. See id. (citing Federal Bureau of Investigation, Uniform Crime Reports, Supplementary Homicide Reports, 1993–1997).
29. Id. at 14.
30. Id. at 14–15, Table 4.
31. N.Y. Penal Law § 265.35(3). Shotguns having barrels less than 18 inches, rifles having barrels less than 16 inches, or any weapon made from a shotgun or rifle having an overall length of less than 26 inches must be licensed. N.Y.C. Admin. Code §§ 10-303(1)(a).
32. National Report at x.
33. N.Y.C. Admin. Code §§ 10-303(a), (b).
34. Id. §§ 10-303(b), (c).
35. Id. § 10-303(c).
36. Id. 10-303(f).
renewed, without further investigation, unless the police commissioner has reason to believe the applicant’s status has changed since the prior permit was issued.37

Just as New York State requires every firearm that is purchased to be recorded both on the purchaser’s license and in the State Police database, New York City requires that all rifles and shotguns be registered with the Police Commissioner.38 Within seventy-two hours of the transfer of ownership of a rifle or shotgun, the seller is obligated to report the disposition of the weapon to the Commissioner, along with the permit numbers of both the seller and purchaser, and the make, caliber, type, model and serial number of the rifle or shotgun.39 The evidence suggests that New York City’s requirement of both licensing and registering rifles and shotguns may reduce the likelihood of criminals and juveniles possessing these guns.40

New York City further mandates that only people 18 years and older may obtain a license to purchase and possess a rifle or shotgun.41 The restriction appears effective. In the United States as a whole, 13% of long guns used in commission of a crime during 1999 were traced to juveniles.42 In New York City, by contrast, only 7.8% of such guns were traced to juveniles.43

New York State, therefore, should extend its firearms licensing requirements to long guns, using New York City regulation as its template. Specifically, state law should require that all purchasers of long guns obtain a license to own such a gun; register each gun with local law enforcement authorities; and notify authorities of any transfer of ownership, theft, or loss of the gun within a specified time period. Failure to comply with these requirements should lead to an automatic and permanent loss of the right to obtain a license for any firearm. Additionally, the law should

37. Id.
38. Id. § 10-304.
39. Id. § 10-304(e).
40. A recent study by researchers at the Johns Hopkins Bloomberg School of Public Health’s Center for Gun Policy and Research found that states that require both licensing and registration of handguns make it more difficult for criminals and juveniles to obtain guns from within the state than in states that only require either licensing or registration. Study: Firearms Licensing, Registration Deters Criminals, Juveniles, The Gazette Online, The Newspaper of the Johns Hopkins University, available at http://www.jhu.edu/ngazette/2001/10sep01/10deters.html (Sept. 10, 2001).
41. N.Y.C. ADMIN. CODE § 10-303(a) (1).
42. See National Report at 10.
43. Id. at 11.
require that the loss or theft of any firearm, rifle, or shotgun be reported to the police within twenty-four hours.\(^{44}\)

Furthermore, as in New York City, an unlicensed person should be required to wait up to a period of thirty days before a license is issued and a rifle or shotgun can be legally purchased.\(^{45}\) The licensing system for long guns also should include a background check to ensure that the applicant is not an ineligible purchaser.

Finally, New York State should re-examine the sale of rifles, shotguns and other long guns to juveniles. The dangers of mishandling or misusing any kind of gun are exacerbated by poor judgment, which is reasonably assumed to correlate with age. In New York State, while it is currently unlawful to sell a rifle or shotgun to a minor under the age of sixteen,\(^{46}\) it is legal for a minor to purchase or possess such a weapon if he is in possession of a valid hunting license.\(^{47}\) The statistics from New York City suggest that imposition of a statewide age requirement of at least sixteen years for possession of a long gun—regardless of the possession of a valid hunting license—would lower juvenile criminal use of these dangerous weapons. In addition, the requirement should be raised to eighteen years of age if the individual does not possess such a valid hunting license.

3. Safety Training

California prohibits purchasing or receiving a handgun without a Handgun Safety License issued upon successful completion of a safety test. In New York State, however, only Westchester County requires applicants for a gun license to complete a safety training course prior to being approved for a license.\(^{48}\) The New York Senate has proposed legislation to extend this requirement statewide. We recommend that New York require that all applicants take a gun safety training course and successfully pass a safety test as a condition for obtaining a license.

II. SPECIFIC MEASURES TO RESTRICT IMPROPER ACCESS TO OR HANDLING OF FIREARMS

A. Safe Storage Laws

At least seventeen states have in place what are known as safe storage

\(^{44}\) N.Y. Penal Law \$ 400.10(1).

\(^{45}\) N.Y.C. Admin. Code \$ 10-303(e)(1).

\(^{46}\) N.Y. Penal Law \$ 265.05(6).

\(^{47}\) Id. \$ 265.05. Minors younger than 14 years of age may not obtain a hunting license or permit. N.Y. Envtl. Conserv. Law \$ 11-0929 (McKinney 2000).

\(^{48}\) N.Y. Penal Law \$ 400.00(4-b).
or child access prevention ("CAP") laws. In essence, these laws impose criminal and, in certain states, civil liability on any firearm owner who negligently stores a firearm to which a child gains access and uses to injure or kill himself or another person.\textsuperscript{49} The principal purpose of such laws is to prevent accidental shootings in the home, but interest in their value in preventing intentional shootings by teenagers outside the home has increased in the wake of well-publicized school shootings that have occurred over the last several years.\textsuperscript{50} While legislators in New York State have introduced CAP bills in the past, the Legislature has not passed such a law to date.

Academic research on the effectiveness of CAP laws is quite limited, in part because the first CAP law was not passed until 1989 in Florida. One study of twelve states with CAP laws in place for at least one year found a 23\% reduction in accidental firearm-related deaths among children under 15.\textsuperscript{51} It is also possible, but unproven, that CAP laws also reduce the number of guns in illegal circulation by preventing them from being stolen by intruders.\textsuperscript{52} However, some studies have questioned the


\textsuperscript{50} See id. (discussing shooting at school in Jonesboro, Arkansas). Thankfully, New York State has not suffered such large-scale school shootings in recent years. Researchers have also identified the prevention of adolescent suicide as another objective served by these laws. See Andrew J. McClurg, The Public Health Case for the Safe Storage of Firearms: Adolescent Suicides Add One More "Smoking Gun," 51 HASTINGS L.J. 953, 972-99 (2000) (summarizing research showing link between suicide and firearms stored in the home and extent of unsafe firearms storage).

\textsuperscript{51} Peter Cummings & Frederick P. Rivara, State Gun Safe Storage Laws and Child Mortality Due to Firearms, 278 J.A.M.A. 1084, 1085 (1997); see also McClurg, supra note 49, at 57 (discussing this study).

\textsuperscript{52} The connection between crime guns and gun theft is a subject of intense and unresolved debate. See McClurg, supra note 49 (reviewing theft statistics). The significance of illegally possessed firearms that were, at one time, stolen from owners who legally possessed them is disputed. While it is beyond dispute that substantial number of guns are obtained by criminals in this manner, what is less clear is whether those same criminals would have had access to a gun in any event and whether the firearms-related crimes they committed would thus have occurred regardless. Compare id. (arguing that reducing the sizable numbers of stolen guns possessed by criminals should reduce firearms-related violence) with Gary Kleck, Policy Lessons From Recent Gun Control Research, 49 LAW & CONTEMP. PROBS., No. 1, at 57 (1986) (concluding from surveys conducted of criminal inmates that because criminals can obtain firearms without stealing them, theft statistics do not mean that reductions in firearms-related crime would follow from reducing firearms ownership generally).
effectiveness of these laws, and suggest that safe storage requirements pre-
vent the defensive use of firearms to the detriment of law-abiding victims
of crime. Finally, there is evidence that prosecutors choose not to prose-
cute offenders under CAP laws, although that does not mean that these
laws are not, to some significant degree, self-enforcing.

With the exception of Hawaii, all state CAP laws impose criminal
liability for negligent storage of a loaded firearm only. There is no solid
policy reason for this limitation on liability because a child or teenager
may obtain access to an unloaded firearm and ammunition in the home,
with deadly consequences.

Similarly, most states’ CAP statutes do not apply if the child who
caused the injury was more than sixteen. Yet, while the risk of acciden-
tal injuries presumably decreases with an increase in the child’s age, the
threat of intentional injuries may increase or at least remain constant. A
statute that imposed liability for negligent storage of a firearm used inju-
riously by a shooter of any age would increase incentives for safe storage
even for owners without children in the home. Any CAP statute passed in
New York State should therefore not be limited to incidents involving
children under age sixteen.

The various CAP laws across the country, as well as the federal legisla-
tion introduced but not passed in 1998, enumerate several defenses to
conviction. These include: a “safe storage” defense, applicable, for ex-
ample, if the gun was stored in a locked firearm safe; an “illegal entry”
defense, applicable if the child gained access to the firearm because of

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53. John R. Lott, Jr. & John E. Whitley, Safe Storage Gun Laws: Accidental Deaths, Suicides, and
2000); see also Daniel D. Polsby, Firearms Costs, Firearms Benefits and the Limits of Knowl-
provable correlations between access to firearms and crime).

54. That may be in part because offenders have often already suffered extreme loss as a result
of the shooting in question. John Lott, Jr., More Guns Less Crime 292 n.9 (University of Chicago


56. Iowa, Virginia, and Wisconsin law cover only children under fourteen years of age;
California, Florida, Hawaii, Maryland, New Jersey, and Rhode Island law cover children
under sixteen years of age; Texas law covers children under seventeen years of age; and
Minnesota, Nevada, and North Carolina law cover children under eighteen years of age. Id.

57 The federal legislation was introduced by Senator Kennedy and Representative Carolyn McCarty.

58. Id. at 64-66. These defenses do not appear to have been fully tested or interpreted yet, as
prosecutions under CAP laws have been virtually non-existent to date.
burglary or other unlawful entry; and a “close proximity” defense, applicable if the firearm was carried by the defendant on his person, or within close proximity, when the child obtained access to it. Such defenses appear to eviscerate some of the principal benefits of a CAP law and should be included in a New York law sparingly, if at all.

Although only Nevada’s CAP law expressly provides for civil liability, it has been argued that courts could find negligence per se following a criminal violation. Civil sanctions may be preferable, given the general reluctance to impose criminal penalties for negligence. Civil actions may also provide a valuable avenue for victims or their families to obtain redress, particularly where prosecutors choose not to prosecute the owner of the firearm. Accordingly, a New York CAP law should provide for a private right of action and civil damages in addition to criminal penalties.

Since 2000, New York has required all firearms sold in the State to have a child safety trigger lock. No weapon may be sold without a locking device and the following accompanying statement:

The use of a locking device or safety lock is only one aspect of responsible firearm storage. For increased safety firearms should be stored unloaded and locked in a location that is both separate from their ammunition and inaccessible to children and any other unauthorized person.

While commendable, this requirement does not address the mass of firearms already owned by New Yorkers. Nor does it cover guns purchased outside New York but stored within the State. A CAP law could encompass these. Moreover, this law does not require the actual use of the trigger lock or the safe storage of guns once they are purchased. In New York, 38% of owners either fail to lock their firearms or fail to keep ammunition in a separately locked location. In addition, it is unclear that the

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59. Id.
60. Id. This defense appears only in California’s statute.
61. Id. at 73.
62. N.Y. Gen. Bus. Law § 396-ee (McKinney 1998). Additional safety standards may be established by the superintendent of the state police with regard to the manufacture, assembly, storage, shipment, and quality of firearms. N.Y. Penal Law § 400.00(12-a).
64. 4 Bradley Hutton & John Fuhman, New York Dep’t of Health, Firearm Ownership and Safe Storage in New York State (Winter 1996).

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required locks provide the same level of safety as gun safes or other security devices likely to be used by owners facing potential liability under a CAP law. For these reasons, the need for a CAP law in New York remains intact despite passage of the 2000 legislation.

We recommend that New York adopt an aggressive CAP law that imposes both civil and criminal liability for the negligent storage of a firearm leading to the injury or death of a person. This law should apply regardless of the age of the shooter; create a private right of action for the victim or his estate to impose civil liability and obtain damages against the negligent party; and allow for only limited affirmative defenses that the firearm was obtained by the shooter as a result of burglary or theft from the owner.

New York should also strengthen its regulation of firearm storage safety. In 2001, the New York State Assembly introduced the Safe Gun Storage Act. Among this legislation’s key provisions are regulations mandating that gun owners lock firearms in a storage unit or, alternatively, use a safety locking device to render firearms incapable of being fired. The Safe Gun Storage Act would further require that firearms sellers inform new purchasers about the safe storage law by including a warning with the firearm. Penalties for violations would be quite limited, with most violations constituting Class A misdemeanors and aggravated violations constituting Class E felonies. The Assembly has not voted on this legislation. If signed into law, this or similar legislation could substantially improve firearm safety.

B. A One-Gun-A-Month Law

New York does not currently limit the number of weapons that may be purchased at one time by an individual. However, the evidence strongly suggests that the State should act to restrict such multiple sales.

According to the ATF, some 22% of all guns used in the commission of a crime and recovered in 1999 were originally part of multiple purchases. The ATF has also found that handguns sold in multiple sales accounted for 51% of all trace guns with obliterated serial numbers.

Four states—Maryland, California, South Carolina and Virginia—limit gun purchases to one gun a month. Virginia’s law, passed in 1993, produced dramatic results. The percentage of New England crime guns originating in Virginia dropped from 35% to 16%. Similarly, the number

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67. Id.

68. Garen J. Wintemute, The Future of Firearm Violence Prevention: Building On Success,
of handguns seized in Washington D.C. that originated in Maryland dropped from 20 to zero after Maryland passed the same law.\textsuperscript{69} One-gun-a-month laws clearly have an effect of stemming the tide of weapons being brought into New York from states with weaker gun laws.

Opponents of such laws argue that their right to purchase guns should not be curtailed. However, the clear and proven benefit of curtailing gun trafficking outweighs the inconvenience imposed by a limit of 12 purchased guns a year. Of the crime guns traced in New York in 1999, nearly a fifth originated within the state.\textsuperscript{70} Over 72\% of those guns were used and seized outside the county of purchase.\textsuperscript{71} Although there are no statistics by which to determine how many of the guns that migrated across county lines were originally part of multiple sales, a one-gun-a-month law in New York would curtail some of this cross-county migration.

Accordingly, we recommend that New York State adopt a one-gun-a-month law to curtail the ultimate illegal use of firearms. Exceptions to the law can allow for replacement of lost or stolen handguns, permit purchases by law enforcement or security personnel, and protect trade in antique weapons.

\textbf{C. Ballistic Fingerprinting of Long Guns}

As noted, every sale of a firearm within New York State requires that the parties provide certain information to the State Police. The purchaser must provide his license to local law enforcement officials, who then provide documentation for the purchaser to show to the seller as proof that he possesses a valid license. Once the purchase is complete, the purchaser must register the firearm in question with local officials. All gun dealers must maintain a record of the date the gun was sold, the name, age, occupation, and residence of the purchaser, and the caliber, make, model, manufacturer's name and serial number, or any other distinguishing characteristics of the weapon, and forward that record to the state police within ten days of sale.\textsuperscript{72} Upon
sale or delivery of any pistol or revolver, the dealer must also forward to the police a sealed container with a shell casing from the pistol or revolver to be entered in the State's electronic ballistic identification databank, a process known as “ballistic fingerprinting.”

In the wake of the sniper shootings in the Washington, D.C. area in 2002, advocates in New York have called upon the State Legislature and Governor to extend the State's ballistic fingerprinting law to cover long guns as well as just firearms, as currently defined. In addition, United States Senators Schumer and Kohl have introduced federal legislation to establish a national ballistic fingerprint database to assist law enforcement officials in identifying shooting suspects. In conjunction with our other recommendations for enhanced regulation of long guns, we recommend that state law require long guns to be “fingerprinted” in this fashion, thus assisting law enforcement authorities in identifying and prosecuting criminals who use weapons illegally.

D. Ammunition Magazines

Federal gun laws have long taken into account the importance of regulating ammunition. The federal Gun Control Act includes comprehensive provisions relating to ammunition control. The transfer and possession of high-capacity ammunition feeding devices are prohibited, and a knowing violation of the law's ammunitions control provisions is ground for fines or imprisonment up to five years.

New York law currently tracks federal law in banning high-capacity ammunition magazines that carry over ten rounds. Both the federal and New York bans, however, apply only to magazines manufactured after 1994. New York should extend its ban to all magazines of this kind, regardless of their year of manufacture. An exception should be included for antique firearms.

74. 18 U.S.C. § 922(w)(1). Again, the provision is not retroactive. 18 U.S.C. § 922(w)(2). Regulation extends to weapons with a high ammunition capacity. Thus, possession of a semiautomatic assault weapon during and in relation to any crime of violence or drug trafficking crime is subject to a minimum sentence of ten years. Id. § 924(c)(1)(B)(i). The minimum sentence increases to 25 years for a second conviction. Id. § 924(c)(1)(C)(i). California also prohibits the sale or transfer of ammunition magazines capable of holding more than 10 rounds. California Enacts Nation’s Strongest Assault Weapon Ban, Limits Handgun Purchases, U.S. Newswire, July 19, 1999.
75. 18 U.S.C. § 922(w)
76. Id. § 924(c)(3).
E. Assault Weapons, “Junk” Guns, and Sniper Rifles

Several classes of guns are so dangerous, and have such limited purpose beyond the commission of violent crime, that they should be subject to increased regulation. There are several steps New York should take in this respect.

First, it should consider broadening the current ban on assault weapons. In September 1994, Congress passed the Violent Crime Control and Law Enforcement Act of 1994 (“the Anti-Crime Act”), which banned assault weapons.77 Codified at 18 U.S.C. § 922(v), the ban prohibits the manufacture, transfer, and possession of certain semiautomatic assault weapons.78 The Act provides the first and only national statutory definition of an assault weapon. The term “semiautomatic assault weapon” means any of the firearms,79 or copies or duplicates80 of the firearms in certain listed calibers (including the Beretta AR70 and the Colt AR-15); semiautomatic rifles81 and semiautomatic pistols that have an ability to accept a detachable magazine and have at least two listed, enhancing features; and semiautomatic shotguns that have at least two listed, enhancing features.82 In addition to creating a statutory exemption for firearms that are manually operated, permanently inoperable or antique,83 and for semiautomatic rifles or shotguns that cannot hold more than five rounds of ammunition,84 the Act also expressly exempts over 650 conventional sporting firearms.85

New York law presently follows federal law by adopting the federal

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77. Pub. L. No. 103-322 § 110102 (1994). The assault weapons ban is scheduled to "sunset" in September 2004 if it is not renewed by Congress.
78. It does not apply to assault weapons lawfully possessed at the time of enactment. 18 U.S.C. § 922(v)(2).
79. The term "firearm" means "(A) any weapon (including a starter gun) which will or is designed to or may readily be converted to expel a projectile by the action of an explosive; (B) the frame or receiver of any such weapon; (C) any firearm muffler or firearm silencer; or (D) any destructive device. Such term does not include an antique firearm." 18 U.S.C. § 921.
80. The ban on "copycat models" seeks to ensure that minor alterations in the manufacture of the designated weapons will not slip through unforeseen loopholes. BUREAU OF ALCOHOL, TOBACCO AND FIREARMS ASSAULT WEAPONS PROFILE 1-17 (1994).
81. A "semiautomatic rifle" is any repeating rifle which utilizes a portion of the energy of a firearm cartridge to extract the fired cartridge case and chamber the next round, and which requires a separate pull of the trigger to fire each cartridge. 18 U.S.C. § 921(a) (28).
82. Id. § 921(a) (30).
83. Id. § 922v(3) (B)
84. Id. §§ 922v(3) (C), (D)
85. Id. § 922(v) (3) (A & App. A.)
definition of “assault weapon.” Firearm safety advocates have argued that this definition is too narrow, and should be broadened to include any firearm that has even one specified military feature such as a pistol grip. We recommend that the State conduct a comprehensive study of weapons used in crimes within New York to determine if the ban should be broadened to include additional weapons.

A second class of firearms whose sale should be legally banned is comprised of so-called “junk” guns. These handguns are easily concealed and particularly accessible to criminals because of their low cost. In 1993, 8 out of 10 guns confiscated by the police in California were classified as junk guns. In addition, their shoddy manufacture makes these firearms a serious danger to their owners. They frequently misfire, fire accidentally or backfire. A metal alloy body also makes the guns melt at a much lower temperature than typical steel firearms and thereby frustrates police efforts to identify these guns through ballistics and serial numbers.

At least eight states have banned small “junk” handguns, otherwise known as “Saturday night specials,” most recently Massachusetts in 2000. The Massachusetts ban only allows junk guns to be sold if they pass a series of test fires of 600 rounds and a drop test to ensure that they will not fire when dropped. The State of California passed a ban with test requirements similar to Massachusetts’ along with the additional requirement of a safety device to prevent accidental discharge.

After Maryland passed its ban, the state saw a decrease in the proportion of gun crimes involving this type of handgun. It remains unclear, however, what impact these bans have had on overall rates of firearms-related crime. Critics argue that bans on such handguns simply encourage criminals to substitute larger and thus more deadly guns for the smaller weapons.

89. Id. at 311.
90. AP Newswire, Massachusetts Institutes Tough New Gun Laws, But Foes Point to Regulations Already In Place, St. Louis Post-Dispatch, Apr. 4, 2000, at A3.
91. Stricker, supra note 88, at 313.
92. Wintemute, supra note 68, at 476.
93. See, e.g., Kleck, supra note 52, at 49-50 (substitution effect and greater deadliness of long guns argues against bans on handguns alone or Saturday night specials in particular).
weight of evidence nevertheless suggests that the added dangers posed by easily-concealed "junk" guns outweighs the impact of any substitution effect. Accordingly, New York should follow other states in banning these guns entirely, or requiring testing similar to that required in Massachusetts and California prior to their sale.

III. PROPOSALS TO EXPAND AND ENFORCE LIABILITY FOR IMPROPER MANUFACTURE, SALE, OR POSSESSION

A. Civil Liability for Secondary Sales to Ineligible Purchasers

The federal Gun Control Act of 1968, which established the foundation for the current regulatory approach taken by the federal government toward guns, centered its efforts on the sellers of firearms. The Gun Control Act established a licensing system that requires all persons intending to engage in the business of selling firearms to become federal firearms licensees or "FFLs." The Gun Control Act also makes it unlawful for any licensed dealers to sell "any firearm to any person who the licensee knows or has reasonable cause to believe does not reside in . . . the State in which the licensee's place of business is located." A person who seeks to purchase a handgun from an FFL must provide the dealer with written assurance that he is not ineligible under the law. The FFL faces criminal liability if he makes a sale without obtaining such an assurance, or knowingly sells a firearm to an ineligible person. The Act does not require that the FFL verify the buyer's purported place of residence, however, making it virtually impossible to prove a violation of this particular provision.

In 1993, federal legislation known as the Brady bill attempted to enhance federal regulation of handguns by imposing a waiting period on all handgun sales. Specifically, the Brady bill required that FFLs delay a handgun sale for up to five business days for a background check to be

94. Id. at 51.
95. 18 U.S.C. §§ 922, 923(a). Individuals may sell firearms without a license, but must not sell to ineligible persons as defined below. Needless to say, the federal licensing system does not even cover all legal gun sales. See generally James B. Jacobs & Kimberly A. Potter, Keeping Guns Out of the "Wrong" Hands: The Brady Law and the Limits of Regulation, 86 J. CRIM. L. & CRIMINOLOGY 93, 94-96 (1995) (summarizing provisions of federal law).
96. 18 U.S.C. § 922(b) (3).
97. Id. §§ 922(a) (1) (A), (3).
98. Id. §§ 924(a) (2), (3).
performed by the chief law enforcement officer in the dealer’s jurisdiction.\textsuperscript{99} The Brady bill required the FFL to obtain from the prospective buyer a written statement affirming that he is not ineligible and photo identification and, if satisfied, to forward this information and a completed “Brady form” published by ATF to the law enforcement officer within one business day.\textsuperscript{100} The purchase could then only be consummated if the officer indicated that the prospective buyer is not ineligible under the law, or if the waiting period passed without a response from the officer.\textsuperscript{101} The chief law enforcement officer needed only to “make a reasonable effort” to ascertain whether the prospective buyer was ineligible.\textsuperscript{102}

In June 1997, the U.S. Supreme Court struck down on Tenth Amendment grounds that portion of the Brady bill which required state or local law enforcement agencies to conduct background checks.\textsuperscript{103} While some localities stopped performing such checks, all but two states (Ohio and Arkansas) agreed voluntarily to continue performing this service in aid of the federal regulatory scheme.\textsuperscript{104} The Brady bill’s waiting period provision itself included a sunset provision that ended the federal requirement as of December 1, 1998, but the law continues to require that FFLs obtain the results of an instant background check through a nationwide database managed by the Federal Bureau of Investigation.\textsuperscript{105}

Gun control advocates claim that the Brady bill has kept handguns out of the hands of hundreds of thousands of ineligible purchasers. In 1995, ATF completed a survey that concluded that, in one year, the law had prevented an estimated 41,000 ineligible persons from obtaining handguns through the background check system.\textsuperscript{106} Commentators have ques-

\begin{footnotesize}
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\item \textsuperscript{99} 18 U.S.C. § 922(o)(1)(A).
\item \textsuperscript{100} 18 U.S.C. § 922(o)(3).
\item \textsuperscript{101} 18 U.S.C. §§ 922(o)(1)(A)(i)-(iii).
\item \textsuperscript{102} 18 U.S.C. § 922(o)(2).
\item \textsuperscript{103} Printz v. United States, 117 U.S. 2365 (1997).
\item \textsuperscript{104} Jens Ludwig & Philip J. Cook, Homicide and Suicide Rates Associated with Implementation of the Brady Handgun Violence Prevention Act, JAMA 2000; 5:585 at 2; Lott, supra note 54, at 292 n.9.
\item \textsuperscript{105} Ludwig & Cook, supra note 104.
\item \textsuperscript{106} See Jacobs & Potter, supra note 95, at 103-4 (discussing BATF study); see also Wintemute, supra note 68, at 475 (citing statistics showing that 70,000,000 ineligible persons are prevented from purchasing handguns each year); Jill A. Tobia, The Brady Handgun Violence Prevention Act: Does It Have a Shot at Success?, 19 Stan. J. Envt’l. L. 894, 904-07 (1995) (summarizing debate on effectiveness of waiting periods).
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tioned such claims both because some of the prospective purchasers who were initially rejected were later approved after additional paperwork was provided and, more importantly, because there is little evidence to suggest that those who were rejected through Brady-required background checks did not simply obtain a handgun by other means. Indeed, research suggests that as many as five out of six felons who own handguns obtained them from the secondary market (i.e., a sale from the first retail purchaser to a second buyer) or by theft, and not from an FFL.107 In other words, it remains far from clear that, even if states continue to conduct background checks, such regulation translates into reductions in handgun-related crime. In fact, the authors of the only true regression study analyzing the full period since the Brady bill became effective found no reduction in homicide rates resulting from the Brady bill’s waiting period.108

One weakness of the federal licensing scheme is the low threshold for obtaining an FFL license in the first place. The ATF must approve an application to become an FFL if the applicant asserts in a written application that he or she is not ineligible to purchase or possess firearms, provides certain basic identifying information including a photograph and fingerprints, and pays a minimal fee of $200.109 The majority of FFLs are not true businesses, but simply individuals who wish to be able to obtain unlimited firearms through the mail.110 While the ATF conducts occasional inspections of gun stores, few resources have been devoted to ensuring that FFLs selling out of their homes comply with the Brady bill at all.111 Significantly, when the Brady bill was passed, Congress chose not to provide any additional resources to the ATF to enforce its new requirements. As an unfunded mandate, the Brady bill’s promise has rested entirely on state and local law enforcement officers who have responded in part by successfully challenging this burden in court. Not surprisingly, federal licensing of firearms dealers currently does little to prevent FFLs from illegally selling firearms to ineligible persons and across state lines.

107. Id at 104-5 (discussing survey conducted by National Institute of Justice among felons in prison); see also Id, supra note 54, at 109 (finding no reduction in crime resulting from Brady); Philip Heymann, The Limits of Federal Crime-Fighting, Wash. Post, Jan. 4, 1997, at C7 (concluding Brady not responsible for crime reductions because “most guns were never bought by youth from licensed gun dealers”).
108. Ludwig & Cook, supra note 104.
111. Id
Most importantly, the federal regulatory scheme does not reach the secondary market for firearms, where the vast majority of criminals obtain their weapons. Nor does it prevent “straw purchases” by eligible persons for ineligible friends, relatives, or associates. While laudable as a symbolic first step in nationwide gun control, therefore, Brady did not address the principal source of firearms for criminals.

Nor has New York law fully filled that gap. Under New York law, rifles, shotguns, and firearms may be sold by licensed dealers either on licensed premises or at a gun show. Dealers must renew their licenses at least every three years, and they are also charged with fulfilling several other requirements in the sale of a gun. But even though the secondary sale of a firearm without a dealer’s license is a felony, such sellers escape arrest and prosecution for the most part. Neither federal nor state law addresses this problem.

One way to help fill this gap is through the creation of a civil right of action that would create liability for someone who sold a firearm in violation of the law. In 2002, Assemblyman Peter Grannis introduced a bill that would create a civil right of action on behalf of a person injured or killed by a firearm against a person, firm, or corporation who sold or transferred such firearm in violation of applicable state or local laws prior to the date of injury or death. This proposal would create an added disincentive against illegal secondary sales and could provide valuable financial and emotional recompense for a victim’s injuries.

B. Facilitating Litigation Against Firearms Manufacturers and Distributors

In 2000, the Attorney General of the State of New York filed suit against various firearms manufacturers and distributors in New York State Supreme Court, asserting among other things that the defendants’ manufacture and marketing of firearms without adequate protections against sales to criminals produced a public nuisance. The defendants filed a motion to dismiss the complaint.

113. N.Y. Penal Law § 400.00(10).
115. See Kleck, supra note 52 at 58-59 (recommending this approach).
116. People v. Sturm, Ruger & Co., 8/17/2001 N.Y.L.J. 18 (col. 1); see also John G. Culhane & Jean Macchiaroli Eggen, Defining a Proper Role for Public Nuisance Law in Municipal Suits...
On a parallel but closely related front, numerous firearms manufacturers found liable for negligent firearms marketing and assessed damages on a market-share theory by a jury in the United States District Court for the Eastern District appealed that verdict to the Second Circuit. The Court of Appeals for the Second Circuit then certified two questions to the New York Court of Appeals. In answering those questions, the Court of Appeals rejected the market-share theory of damages and, more significantly, held that the manufacturers' duty of care did not extend to the general public without more. In order to prove such liability for negligence, the Court found that a tighter nexus of causation must be shown between the firearms produced and distributed by the defendants and those actually used to shoot the plaintiffs. Without that clearly delineated nexus, the finding of liability against the defendants would, in essence, hold them liable for the intervening criminal acts of an unrelated third party. Following this decision by the New York State Court of Appeals, the Second Circuit reversed the verdict in Accu-Tek. Justice York, in turn, dismissed the Attorney General's complaint in Sturm.

Although the outcome of Sturm on appeal to the Appellate Division remains uncertain, these decisions suggest that the Legislature and Governor could remove at least some of the barriers to success imposed by common tort law. Some commentators have proposed imposing strict liability on firearms manufacturers using this tort doctrine as it has been applied to ultra-hazardous activity in the past. A more fruitful approach would be to define more clearly in statute the nature of the proof of causation needed to hold manufacturers, wholesalers, and dealers liable for negligence in marketing firearms or for the creation of a public nuisance. Any

Against Gun Sellers: Beyond Rhetoric and Expedience, 52 S.C. L. Rev. 287, 301-10 (2001) (summarizing public nuisance claims brought by municipalities and explaining theory behind such claims).


such approach should be narrowly tailored. Public debate over this issue would serve to determine popular support for expanded litigation against the firearms industry. If adopted, legislation to guide courts and juries in handling such cases could provide a critical avenue to limit the flow of illegal firearms into New York State.

IV. INTERDICTION OF FIREARMS TRAFFIC FROM OTHER STATES
In an effort to stop the flow of illegal guns into New York from so-called “supplier” states New York adopted a gun trafficking interdiction program in 2000.123 The program’s strategies includes authorization and limited funding for New York district attorneys to enter into collaborative agreements with ATF and law enforcement agencies in supplier states to identify and prosecute gun traffickers who bring guns into New York State. The legislation also requires that the State police establish a central repository of information on all guns believed to have been used in the commission of a crime, and that State and local law enforcement coordinate with ATF to trace the origin of such guns.

In early 2001, Governor Pataki established the Special Weapons Interdiction Field Team (“SWIFT”), an elite division of the State Police focused on interdiction of illegal firearms. SWIFT analyzes gun trafficking patterns and is charged with establishing formal working agreements with the ATF and local law enforcement in states that supply illegal guns to New York.

Despite substantial progress in tracing guns used in crimes in New York State, these initiatives have been hampered by limited state funding. Without complete, accurate tracking and reporting of seized firearms by localities, the data used to monitor the origins of crime guns are insufficient. Similarly, resources are needed to investigate and prosecute these cases.124 Accordingly, we recommend that additional resources be devoted to the State’s existing interdiction efforts.

V. CONCLUSION
New York State substantially regulates the possession and use of firearms, but these regulations have important shortcomings that could be

solved through reasonable changes in the law. Such changes must be aimed at all stages of the life of a firearm, from production to possession.

State licensing requirements should be changed to require gun owners to renew their firearms licenses periodically, to require licenses for rifles, shotguns and other long guns, and to require safety training and testing prior to approval for a license. Although these changes will help law enforcement officials track legally owned firearms, it is also important to regulate the manner in which these weapons are stored and handled. Accordingly, we recommend the passage of a safe storage law, a one-gun-a-month law, a law requiring the ballistic fingerprinting of long guns, a study to determine whether the existing ban on assault weapons should be broadened, and a ban on “junk” guns.

In order to ensure that a more stringent licensing regime and increased regulation of firearms can be successfully implemented, these efforts should be combined with laws that expand the scope and enforcement liability for the improper manufacture and sale of firearms. And finally, to ensure that internal regulations are not thwarted by the continued influx of illegal guns from outside New York State, existing interdiction programs should be fully funded.

By adopting the measures recommended above, the State of New York could take giant strides to ensure that guns are manufactured and distributed legally, stored safely, monitored accurately and used properly. The public benefits of such reasonable reforms cannot be understated.

January 2003
The Committee on State Affairs
Jeremy M. Creelan, Chair
Bradley A. Siciliano, Secretary

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In Opposition to the Board of Law Examiners’ Proposal to Increase the Passing Score on the New York Bar Examination

The Committees on Legal Education and Admission to the Bar

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In Opposition to the Board of Law Examiners’ Proposal to Increase the Passing Score on the New York Bar Examination

The Committee on Legal Education and Admission to the Bar

Introduction

The Committee on Legal Education and Admission to the Bar of the Association of the Bar of the City of New York submits this Report in opposition to the Report and Recommendation of the New York State Board of Law Examiners to the Court of Appeals Regarding the Passing Standard on the New York State Bar Examination (the “Report”).

At the outset we emphasize that we join the Board in recognizing that any change in New York’s standard for licensure should be rooted in “scientifically based studies informing our policy judgments” (Report at 13). It is because we agree with the Board that there should be both careful scientific analysis and a full consideration of competing policy concerns that this Committee urges that no change be made in the passing score until both its effectiveness in meeting the goals of the Board and its ramifications for those seeking to become lawyers and those seeking legal services have been explored in scientific analyses that go far beyond what may have been learned from the Klein Study discussed in the Report. We believe that the Board’s proposal is likely to have a disparate impact on...
minority candidates, reduce the availability of legal representation to already underserved persons and discriminate among candidates on the basis of financial means—all without a sound basis for expecting that the proposed change will be useful in screening candidates for entry-level competence to practice law.

Accordingly we submit this report: (i) to express the Committee’s opposition to the Board’s proposal to increase the passing score on the New York State Bar Examination from 660 to 675, (ii) to comment on the research conducted by Stephen P. Klein, Ph.D., that is extensively relied upon in the Report, (iii) to suggest additional research that should be conducted as part of any review of the passing score, and (iv) to discuss critical policy considerations relating to the proposal that, in our view, go to the heart of the Board’s gate-keeping function.

In addition, we join with the fifteen New York State Law School Deans in requesting that public hearings be held on this most important matter.1 We note that both Florida and Minnesota, the two states most recently to consider a substantially similar proposal, held public hearings enabling interested parties to testify and present evidence. Given the unquestionable public significance of a proposal affecting access to the legal profession and the availability of legal services, it is certainly appropriate for the Board to give members of the public, including representatives of minority organizations, representatives of the organized bar, deans and law professors, an opportunity to express their views.

The Relevant Standard: Entry-Level Competence

The Board has stated that the “passing standard must accurately reflect the minimum level of competent performance required for admission into the profession” and that the passing score should be both “representative of current norms for minimum competence” and “calibrated to the level which affords the public protection.” (Report at 1.)

Each of these is a laudable, important goal. This Committee has previously expressed its view that the bar examination tests only a few of the many skills and competencies new lawyers should possess in order to competently practice law.2 We repeat our concern that the current examina-

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1. While representatives of the Committee testified at hearings before the Board on February 14, 2003, we were disappointed that these hearings were held on very short notice and that members of the Court of Appeals did not participate in these hearings.

tion addresses only some of those “competencies” and tests them in an artificial setting and manner unlike the actual practice of law. Moreover, while there has been considerable writing and debate on the multiple competencies involved in fulfilling lawyering tasks in a competent manner, there is no independent consensus among practitioners as to the substance of “minimum competence” as measured by the current bar examination. We note that the Board did not seek such a consensus from the panel of practitioners and teachers it assembled as part of the research on which its Report is premised.

Nonetheless we recognize that the Board must perform its duties in the examination of potential lawyers in a context of both limited time and limited resources, and we appreciate that the Board is conducting its current review of the passing score with the goals of testing competence and protecting the public. However, we believe that there has been no showing, in the Report or otherwise, that the current passing score has resulted in the licensing of incompetent lawyers or that setting a higher passing score will protect the public from incompetent lawyers.3

We agree with the Board that the precise passing score will always have some element of the arbitrary and that New York’s passing score of 660 was not set after any scientific study to measure “minimum competence.” (Report at 2.) However as the extensive study commissioned by the Court of Appeals commented in 1993, the 660 passing score does have a “rationale” in that it is based on a historical view taken by Boards of Law Examiners regarding the minimum level of performance for a qualified candidate.4 When the MBE was added to New York’s examination, the pre-1979 passing rate was the basis for setting the passing score at 660. Prior to 1979 the “primary criterion was candidate performance relative to the content of the questions rather than adherence to a group standard consisting of a fixed percentage of passing candidates.”5

But saying that these measures are imperfect, or that the existing baseline was based on long experience rather than scientific study, does not sup-

3. We do agree with the Board that the incidence of disciplinary complaints about competence or malpractice claims is an insufficient measure of whether particular scores measure competence. It might still be useful to know whether bar examination scores correlate with disciplinary proceedings and malpractice claims.

4. Millman, Mehrens & Sackett, An Evaluation of the New York State Bar Examination (1993) (“Millman Evaluation”) at 8-1. The Board confirms that in 1979 it made the assumption that the then-existing passing rate was one practical measure for discrimination based on competence (Report at 2).

port the conclusion, *ipse dixit*, that a candidate who scores 675 (MBE 135) is “more competent” to practice law than one scoring 660 (MBE 132), or that the former is “minimally competent” but the latter is not. To make such a judgment, particularly when those scoring 660 (MBE 132) are currently passed as minimally competent, requires careful analysis of the score scale, the characteristics of those candidates currently scoring between 660 and 675 (or 685, the Board’s longer term target), the explicit and implicit assumptions behind the definition of “minimum competence” the Board chooses to employ, and the connection between differences in test performance and competence in practice.

In these regards we would emphasize that the extensive study commissioned by the Court of Appeals a decade ago recognized that:

>a licensure examination is not an employment examination, nor have any inferences about degrees of success for those who score above the cut score been validated. Thus, there is no evidence that would justify an employer selecting among applicants based on how far they scored above the cut score.6

We agree with the Board on “the importance of engaging in standard setting exercises in determining passing standards, rather than relying on assumptions” (Report at 16). We suggest, however, that “standard setting” means more than adjusting the passing score on the existing examination. Rather, a proposed change in the examination passing score must be evaluated in terms of whether it will better screen for minimal competence or simply increase the short-term pressures of exam preparation. That requires express debate, rather than implicit methodological assumptions, about the content of “minimum competence” and careful analysis and thorough discussion of how the examination may measure such competence (or competencies) and most effectively fulfill its screening function.

Deciding what “level of knowledge and skills [is] deemed appropriate for the entry level practice of law” is a judgment rooted in policy—policies about lawyers, the populations they serve and the structures through which such services are delivered. It appears that the proposal to increase the passing score reflects more than anything else a concern that New York not be perceived as having standards lower than those employed by other states. We believe that New York’s exam is among the most rigorous in the nation. Indeed, some commentators have deemed it to be the most difficult. When comparing New York’s passing score to those adopted in

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other jurisdictions, the Board and the Court of Appeals should bear in mind New York’s extensive testing of mastery of distinctive characteristics of New York law and practice in addition to the testing of “multi-state” substantive law. However one may assess the value of an emphasis on New York law, it seems clear that this already requires a level of post-law school preparation (measured in time and money) not necessary in many other jurisdictions. New York should proudly stand by its commitment to a competent, professional Bar that reflects the great diversity of the State and strives to be available to all who need legal services, rather than act on an apparent desire to compete with other states in terms of whose MBE-driven passing score is the highest.

In making the points which follow we are not arguing against setting standards for admission into the profession. We do not think for a moment that there should not be “any standard at all” (compare Report at 18). Nor are we arguing that an examination should have no role in admission to the Bar. But whether a test is “reliable” in terms of its consistency of administration does not bear on the utility of its scaled score as a relative measure of professional competence, and it is not possible to assess the validity of increments in the scaled score without expressed consensus both on what “minimum competence” means and on what external measures of such competence for future practice may be used to assess the validity of the examination and its scale.

**Impact on Candidates, Racial Diversity, and the Availability of Legal Services**

We are concerned that the proposed increase (i) is likely to have a disproportionate impact on minorities, both candidates for admission and those in need of legal services, and (ii) will undoubtedly increase the time and expense involved in preparation for the examination. (The latter point is addressed in the next Section.) While the Report states that “the Board is advised that an increase in the passing score should have no measurable effect on existing differences among minority and non-minority groups in passing rates on the New York bar exam” (Report at 19-20), it provides neither source nor substance for this “advice.” Moreover, the Board acknowledges that it has not previously collected demographic information, considering such “obviously irrelevant to the pass/fail decision the Board is called upon to make” (Report at 14).7

7. The Report admits, “Evidence that would support or refute that proposition [i.e., the potential for disparate impact on minorities] has not been collected.” (Report at 14). In fact,
It is one thing to admit that because information “irrelevant to the pass/fail decision” has not been collected, the potential for disparate impact cannot be assessed from bar examination data. It is simply erroneous to transform that admission of ignorance into “advice” that there will be no such impact.

The LSAC National Longitudinal Study starkly illustrates the disparities in passing rates among different racial groups of a cohort of 1991 law school enrollees (most of whom would have taken the bar examination for the first time in 1994). The LSAC Study reported eventual passing rates of 77.63% for Blacks and 96.68% for Whites. That Study also established that Black candidates who initially failed the bar examination were somewhat more likely to abandon the process, and not try again. The Millman Evaluation, using New York's July 1992 examination, reported a difference between the mean score for Blacks and Whites of 80 points. The difference in July 1992 New York passing rates was also enormous: 81.6% for Whites, 37.4% for Blacks.

The Report responds to this concern by suggesting that if the proposal to increase the passing score is adopted, a study be commissioned to gather the relevant demographic information in order to assess the impact of the increased score (Report at 14). But surely such a study should be performed before—and not after—the proposed increase goes into effect. It would be a relatively simple matter to collect the demographic data during the next several administrations of the exam and then determine precisely the effect on different groups of increasing the passing score from 660 to 675 (or eventually to 685 as the Board contemplates).

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9. Wightman, LSAC National Longitudinal Bar Passage Study (1998). The LSAC study reported large differences in attrition rates for examination candidates based on race. But see Strickland, The Persistence Facts, AALS Newsletter, Nov. 2000, Page 5, recalculating the LSAC data with respect to attrition to use those initially not passing as the denominator (rather than the pool of candidates). The result (dropouts as a percentage of those initially failing) was 28% for African Americans, 24% for whites and lower percentages for Asian Americans and Latino candidates.
10. Millman Evaluation, Table 10.1 at page 10.4 (regression analysis of a mail-in questionnaire supplies a somewhat narrower but still broad “parameter,” id. at 9-11). The classification labels are those used in the report.
11. Id. at 10-4.
The Committee has learned that Florida collected demographic information in connection with the two administrations of its 2000 bar examination. The data clearly showed that there would have been a disparate impact on minority candidates if the passing score had been raised two or five points, because minority candidates disproportionately scored in these ranges. A passing score increase of 2 points would have failed 4.56% of whites who otherwise passed; a five point increase would have failed 12.33% of whites who otherwise passed. By contrast, 7.57% of minority candidates who passed would have failed if the passing score had been raised two points and 17.1% would have failed if the passing score had been set five points higher.

Our concern about the impact of the proposal is not limited to its effects on candidates; it extends as well to the people who would be deprived of their legal services. There is good reason to expect that the candidates who will not be admitted because of the new passing score would have been more likely to join small firms or enter solo practice, providing legal services to working class and middle class individuals and families. There is evidence that minority lawyers are more likely than other lawyers to provide services to the poor and other underserved groups. With courts increasingly strained by the number of unrepresented litigants, and the pervasive and complex presence of law in the lives of all of us, responsible public policy requires that the supply of legal services to underserved populations not be unnecessarily adversely affected. Further, our concern extends to the negative impact on public trust and confidence in the legal system when those in the courts and the legal profession do not reflect the makeup of the population and also may not be sensitive to issues and concerns of minority groups.

Given New York’s longstanding commitments to increasing the diver-

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12. Minority candidates were about 24.7% of total July 2000 candidates and 21.2% of passing candidates. They were 26.9% of those scoring 131-135. This data was submitted to the Florida Supreme Court in matter SC96869 (which was the Court’s review of the proposal to change the Florida passing score) in documents dated July 23, 2001, and August 29, 2001. Again, the classification labels are those used in the particular report. Blacks were 50% of the Minority candidates at the February 2000 sitting and about 32% at the July 2000 sitting. The results for Blacks in analysis of the February pass rates would be more extreme than that for Minorities as a group, but the results at the larger July sitting were statistically equivalent.

13. The overall July 2000 pass rates at the existing cut offs were 83% (Whites) and 68% (Minority). Because a substantially lower percentage of minority candidates pass, drops in absolute numbers of candidates (e.g., 4.56% versus 5.14% of all candidates upon a two point shift and 10.2% versus 11.63% at a five point shift) have a larger proportionate impact on the cohorts passing the test.
sity of the Bar and to affording legal services to diverse communities, the proposal to increase the passing score should not be implemented in the absence of data demonstrating the relative utility of such an increase and assessing its effect on racial minorities and access to justice. New York's law schools have begun to make noticeable progress in their quest for diversity in admissions. A proposal that runs the risk of disproportionately impacting racial minorities in access to the profession runs the concomitant risk of deterring minorities from even seeking admission to law school.

**Research Predicates**

We doubt that the “standard setting” study conducted for the Board by Dr. Klein (“Klein Study”) demonstrates anything more than the views of the study panel members about the particular essay each panel member reviewed. We note that it is the Board’s stated policy that there “is no passing or failing on any one portion of the examination. . . . Passing or failing is determined only on the basis of the applicant’s total weighted scaled score.” Certainly the Klein study provides no statistically sound basis for extrapolating from views about “passing” one essay question to “passing” the essay portion of the examination (weighted at 40%), let alone a basis for setting the appropriate minimum passing score on the examination as a whole. Our review of the Klein Study persuades us that its resulting recommendation is an artifact of Dr. Klein’s methodology which makes assumptions about “minimum competence” without even attempting to define its meaning. As noted below, the expert panel was not even asked to discuss the criteria of “minimum competence.”

In fact, the Klein Study calls into question the existing practice of scaling the New York components of the examination to the MBE. Research from data available to the Board could address this, and further study of the data collected might also provide the Board with insight into how its guide for grading individual questions compares to practitioners’ assessments of competence. We believe that the Board should systematically address both of these topics before considering the twice-removed question of the appropriate overall passing score.

We respectfully suggest that the policy considerations that underlie any decision to raise the passing score require that the Board provide a persuasive scientific analysis of the benefit of a change in the score. Because the acknowledged purpose of the examination is to test “minimum competence” for protection of the public, we submit that the Board’s scientific review should focus on: (1) developing a substantive standard of “minimum competence” insofar as this involves skills to be assessed
through this examination or any proposed alternatives; (2) how any change in passing score will have a meaningful impact on screening for competence as a practicing lawyer; (3) the population of candidates taking the New York examination and the demographic characteristics of the segment of that population most likely to be affected by the proposed change (i.e., those currently scoring between 660 and 685); and (4) the value of requiring law school graduates to devote even more time and money to preparation for the examination, a factor that necessarily discriminates on the basis of means. We believe that research in each of these focal areas would provide the Board with a wealth of information useful not only in assessing the passing score but also in designing the examination and assessing its function as a standard for licensure.

The Board hypothesizes that further preparation may blunt the effect upon the passing rate of raising the passing score (Report at 10, 13). Others argue both that further preparation would make little or no difference in scores for the candidate pool as a whole and that it is unlikely there would be changes in overall preparation, which we believe is already substantial. Solid research based on several years’ experience in the states which have recently raised their passing scores may provide partial answers—although the New York examination’s heavy emphasis on local law undoubtedly already prompts greater preparation for this examination than is the case in some other states. Even if such additional preparation were to occur in New York as a consequence of a change in the passing score here, it will still be necessary to ask why incremental time spent on examination preparation will benefit the profession or the public and whether the necessity for still-additional post-graduation preparation for an examination would further discriminate among candidates based on financial means.

Although the Board acknowledges that most candidates for admission eventually pass the bar exam, it expresses its conviction that those who pass on a later attempt “are, at that point, better prepared to enter the profession.” (Report at 18.) This Committee noted its disagreement with this assertion some years ago, suggesting it was far more likely that for the later examination, candidates have “improved the narrow range of test-taking skills necessary to pass” without gaining increased competence for practice.14 Before policy changes are made based on the Board’s assertions, follow up studies of those now passing the examination on later attempts and an analysis of such candidates’ initial preparation,

initial score, subsequent preparation and subsequent score should be undertaken to test scientifically the validity of the Board’s assertions. The Board also has the means to conduct follow-up studies about candidates who in past years have scored between 660 and 675 (or 685) on their first attempt to pass the examination. However, we should not lose sight of the fact that the goal must be better preparation for practicing law rather than better preparation for passing an exam.

According to the Board’s analysis of July examination results for 1999-2001, use of the 675 cut-off, absent changes in candidate preparation that resulted in higher scores, would have resulted in between 5.4% and 8.5% of candidates failing rather than passing. Some 12,709 candidates took the Bar examination in 2001 (9,194 in July). The proposed change, then, would have resulted in between 600 and 1000 additional candidates failing in that year. If the net effect of the proposed change is merely to require still-additional preparation before the initial test, then scientific study must inform decision-makers as to the true benefits of this additional cost. If in fact the result of such a change is a decline in the initial pass rate, followed by subsequent successful completion, policy makers must consider on which candidates this burden falls and what the costs and benefits are of deferring admission of these candidates.

The Board’s Report simply does not establish that those who currently score between 660 and 675 lack the “knowledge and skills deemed appropriate for the entry level practice of law.” In what regard does the Board find those candidates lacking? Since we surely do know that raising the passing score will have an impact on the lives of candidates, what measurable benefit will be conferred on the profession or the public?

Comments on Methodology

We appreciate that involving panels of attorneys in a “standard setting exercise” like that conducted by Dr. Klein may provide interesting information about the portion of the examination under study. We do not understand, however, how the results from this exercise can be extrapolated validly into a “passing” grade for the New York essay portion of the examination (were there such a grade, which is not the case), let alone used to set the standard for the examination as a whole.

The Board acknowledges that the methodology followed by Dr. Klein in his study has been seriously challenged when used elsewhere.15 We ap-

preciate that the Board and Dr. Klein have attempted to address some of these critiques. However, the challenges to Dr. Klein’s work are not limited to the kinds of computational alternatives Dr. Klein explores, but go to the fundamental logic of his research protocol.

Because comments on methodology require a level of expertise in the high-stakes testing area that is not otherwise available to the Committee, we have sought the assistance of a quantitative psychologist in preparing the remarks which follow.16

1. From Individual Questions to Overall Essay Assessment

One flaw in the methodology lies in the extrapolation of an ultimate passing rate from averaging the passing rates on individual essay questions. We expressly label this a “flaw” because it represents a methodological tactic which effectively predetermines the result, without first establishing a definition of “minimum competence” that reflects the policy of the Board or even the consensus of the expert panel.

In his study Dr. Klein computes the percentage of applicants who should pass the entire examination by averaging the pass rates for six individual essay questions. More expansively, Dr. Klein’s approach was to determine across the six essays analyzed the average percentage of candidates whose performance on an essay fell below the panelists’/readers’ opinion of minimum competence for that essay. The overall passing score to be set for the composite of all parts of the examination was then calculated to be the total score that would fail the same percentage of candidates as on average “failed” an essay question. Since Dr. Klein’s approach does not rely on an express definition of minimum competence ratified by the Board or the panel, in choosing this methodology, it determines an overall passing score that may or may not satisfy the Board’s intention to set the score to screen for minimum competence. Whether a total score that produces an overall passing rate equal to the average of the “passing” rate for essay questions evaluated by the panels should constitute the standard for “minimum competence” is a very substantial question which the Board did not discuss explicitly, and one which the study panelists were not asked to address.

16. Dr. Jerard Kehoe has a Ph.D. in Quantitative Psychology and has twenty years experience in the development and management of large scale employment testing programs. Among other professional responsibilities, he serves as an Associate Editor of the Journal of Applied Psychology, edited a book on employment testing, and in 2000-2002, served on his professional society’s committee to revise its “Principles for the Validation and Use of Employment Selection Procedures.”
That this methodology represents a tactical choice with policy consequences is made clear by an illustration offered by Carol Chomsky in her testimony before the Minnesota Supreme Court:

Assume I gave an examination consisting of three questions to four students (Alan, Betty, Cindy and Doug) and I decided that they would have to answer two out of three questions correctly to pass. Then assume that the aggregate statistics show that each of the questions was answered correctly 50% of the time. Dr. Klein's methods would result in the conclusion that 50% of the students should have passed the exam and 50% should have failed the evaluation standard adopted. But consider the following two circumstances:

Case 1:
Alan and Betty answered correctly on #1
Betty and Cindy answered correctly on #2
Alan and Cindy answered correctly on #3
Doug answered incorrectly on all 3
In this instance, Alan, Betty and Cindy—75% of the students—passed.

Case 2:
Alan and Betty answered correctly on #1
Alan and Cindy answered correctly on #2
Alan and Doug answered correctly on #3
In this instance, only Alan—25% of the students—passed.

The above illustration shows just one alternative to Dr. Klein's conclusion that performance on the entire examination can be compared to performance on a single question. To offer a different example drawn from statistics in the Millman Evaluation: for the July 1992 examination approximately 55% of candidates got any particular New York multiple choice question correct. Nonetheless 74.6% passed that examination, and the mean score was 705, far above the 660 cut score. Thus the bulk of the examination cannot be thought of in terms of a "passing score" on particular questions—performance must be measured on an accumulated basis.

The methodology that would have been most consistent with the

17. Past-President of Society of American Law Teachers, Professor of Law, Minnesota Law School, Director, Bush Faculty Development Program on Excellence and Diversity in Teaching. The methodological issue illustrated here is discussed at some length in the Merritt Article at 949-62.
current approach to scoring the examination would have been to have the panel score the essays and then have panelists review a sufficient sample of packages of scored essays (each package constituting a candidate’s total essay performance) and evaluate the entire package in terms of whether the candidate had demonstrated minimum competence. This seems more consistent with current practice, which is to use scaled subtotals of scores on various parts of the examination to measure an overall sufficient (on a pass/fail basis) accumulation of knowledge and demonstration of reasoning. Dr. Klein’s methodological assumption introduces a different standard, and that assumption drives its results.

From data already available to the Board it should be possible to analyze the overall performance of the test-takers whose essays were graded by the panels and to learn how strongly their scores on the particular questions correlated with the candidate’s overall performance, both on the essay portion and on the examination as a whole. How, if at all, did achieving this “passing” score on a particular question in fact compare to overall essay performance? How well, if at all, did performance at the margin of the “passing” score on a particular essay in fact predict an overall examination score in the 660-685 range?

If the Board were to accept Dr. Klein’s rationale for recommending a higher passing score, it would be endorsing a passing score without knowing whether the score is proposed based on the method most consistent with its own policies about the profile of test performance that identifies minimum competence. In such circumstances the Board would be allowing a methodological assumption to dictate new policy and would be changing that policy without any expression of consensus within the expert panel, the Board, the Court of Appeals, or the Bar generally that this different policy is appropriate.

We should here note that, in part as a result of questions raised regarding Dr. Klein’s methodology (which we continue to discuss below), the states of Florida and Minnesota apparently have deferred implementation of Dr. Klein’s proposals.

We are also concerned about the sample of answers reviewed and the use of this sample to set a percentage of answers that met or exceeded the panelists’ standard. The average quality of the essays reviewed by the panel appears to have been considerably above the quality of all of the candi-

18. In light of Dr. Merritt’s observations (which are based on statistical analysis of a session of the Minnesota bar examination) we also think it would be valuable to explore the correlation of the quality of applicants’ performance on the variety of New York essay questions, particularly for candidates with overall scores in the marginal ranges.
dates’ essays from that sitting of the 1999 examination as equated through Dr. Klein’s procedures. On Question 4, for example, 57.5% of the answers studied received a score of 2.5 (used by Dr. Klein as the floor for minimum competence) or better from its panel, whereas only 46.1% of the full candidate pool answers were estimated to have met this same standard as recalibrated through a “reader score.” Assuming the arithmetic of recalibration was correct, it appears to us that the sample studied must have quite substantially failed to represent the population of responses. From what we understand, the use of a representative sample is a procedural standard in research on “high-stakes” testing, and the use of a non-representative sample (even if purely by accident) is recognized as a very serious shortcoming.

How the unrepresentative nature of the sample may have affected panel scoring is something we cannot know. We discuss below why the panels’ scoring correlations (which measure relative rankings of essays) do not alleviate this concern. Since sampling differences of the size in the above example exceed the effect of the proposed change in score, we respectfully suggest that this portion of the procedure be reviewed by an independent psychometrician with no prior connection to any of the experts employed by the Board.

Our concerns about this aspect of Dr. Klein’s methodology are reinforced by comparing the Klein Study to the 1993 Millman Evaluation. The Millman Evaluation included a variety of reviews of the examination by local practitioners, including a somewhat similar assessment of essay answers. While the 1993 evaluation’s methodology is open to some of the same criticism as the Klein Study, we are struck by the fact that its panel analysis produced a cut score of 659—some 13 years after 660 had been selected based on historical experience. The Millman Evaluation accordingly recommended that there be no change in the passing score at that time.

We recite this not to commend the methodology of the earlier work, but as the occasion to remark that we cannot imagine what changes in the seven years between the July 1992 examination studied by Millman and the July 1999 examination studied by Klein would lead to such different results. Absent a clear and documented explanation, we are left to suppose that differences in panel preparation or panel composition, use of a “pass rate” methodology, or the unrepresentative nature of the sample are all possible explanations.

One critical difference may be that the Millman Evaluation put more emphasis on defining a standard of minimum competence to be applied by its panel. The 1993 evaluation also used only practitioners on its panels (not full time law professors).\footnote{We do also note that the 1993 exercise was on a smaller scale and reported a margin of error of 18 points because of sample size.} Millman also focused on setting a minimum competence score for each essay rather than using the two-step approach built on passing rates.

Given the importance of the 1993 Evaluation commissioned by the Court of Appeals, we were surprised to discover that it receives only one passing mention in the Board's Report (and none on this topic), and no mention at all in the Klein Study. This particular aspect of the Millman Evaluation did have an element of informality. Nonetheless the wide divergence in results after only seven years warrants a totally independent review of the technical aspects of both studies and an explanation of the difference in results reached.

Michael Kane, Director of Research for the National Conference of Bar Examiners (which administers the MBE), has criticized on a number of grounds the study methodology used by Dr. Klein elsewhere and repeated in New York. Dr. Kane has discussed the proper methodology for “examinee-centered standard setting” in a recent article, and we find one set of his comments particularly pertinent. Dr. Kane believes that while it can be valuable to use panels of academics and experienced practitioners in applying “standard setting” to the examination, because of the relative professional maturity of such panel members, they should have familiarity “with the work of newly admitted lawyers . . . to keep the standard realistic.”\footnote{Kane, Clearing the Bar: Setting the Standard, THE BAR EXAMINER (November 2001) 6, 8.} And once the panel is assembled the next step is critical:

\ldots at the beginning of the standard-setting process, the panelists are expected to reach some level of agreement on a performance standard describing the level of competence required for entry-level practice, which is then used to identify an appropriate passing score. The initial statement of the performance standard can be refined during the study, but it is important to start with a clear focus. The performance standards are likely to be most defensible if they are clearly linked to generally accepted standards of practice.\footnote{Id. at 8.}
This simply did not happen in Dr. Klein’s study. Without in any way disputing the professional qualifications of the panelists, we must point out that the panelists as a group were not asked to reach a consensus on the level of competence required for entry-level practice. Since the panel group included academics as well as current practitioners, the absence of such discussion could only heighten the potential for inconsistency in the scores (as opposed to the relative ranking of essays).

The five panelists considering a specific question did discuss “appropriate criteria for their question” for a passing grade on that one particular question. However, not only was consensus not required, but there is no indication that panelists were focused on “minimum competence” as the standard for “passing.” And clearly the group as a whole did not discuss the qualities of “minimum competence.” It seems to us that a distinctly better job of preparing the panel to evaluate the essays in terms of minimum competence was done in the Millman Evaluation, which recommended no change in the passing score.

As we understand the literature, for a panel procedure like this to be valid it is also necessary that the scoring panel understand the consequences of the scores being applied. The panelists in Dr. Klein’s study were not informed that performance on a particular question would be used as the baseline for constructing a pass/fail measure of competence for the entire two-day test. We suspect that many panelists would at least have questioned, if not rejected outright, this methodology.

Dr. Klein attempts to address this issue by reporting that the panelists’ ratings of the same essays were generally highly correlated with each other, and, to a lesser extent, with the readers’ results. But these correlations only reflect that the panelists were in high agreement about which essay was best, which was second best and so on. These correlations do not provide any evidence of any agreement among panelists and readers concerning the criteria for the assignment of competency ratings or score weights.

One point in gathering practitioners and academics, rather than merely relying on the Board’s existing grading team, surely is to elucidate from a consensus of the panelists what “minimum competence” entails. That requires group discussion of the standard as a predicate to individual grading of sample answers to a single question. Assembly of this group provided a

23. If it is also true in New York, as Merritt reports that studies in other states have shown (Merritt Article at 953-54), that there are relatively low correlations between candidates’ scores across essay questions, then Dr. Klein would not be correct in assuming that the work of the various small panels validate each other in some regard.
striking opportunity to address the standard critical to the Board’s function, the qualities of “minimum competence.” That unfortunately did not happen.

2. From Analysis of the Essay Section to Overall Score

Our second group of methodological concerns turns on the relationship between performance on the New York essay section and the examination as a whole. We appreciate that practitioners asked to make judgments about a “passing” score may feel more comfortable evaluating an essay than picking the number of correct answers on the MBE that seems like “enough” to demonstrate “minimum competence.” However, it is the Board’s present practice to weight the MBE equally with the essays (at 40% each), and to scale each candidate pool’s raw scores on the essays to the MBE distribution. In this section we address the implications of this policy for Dr. Klein’s research and recommendations.

The Millman Evaluation described the essay scoring as follows:

The raw scores (0 to 10) assigned by each reader are converted to standard scores having a mean of 50 and a standard deviation of 10. Thus, the mean and spread of these standard scores are the same for each reader and for each essay question. The average of a candidate’s six essay scores (expressed as standard scores) is computed, and the distribution of these averages is then converted to common-scale values in the same way the NYMC raw scores were converted . . . to common-scale values having the same mean and standard deviation (a measure of variability) as those New York candidates earned on the MBE. For example, if the mean common-scale value for the New York candidates on the MBE is 680, the mean common scale value for these candidates on the [essay] component is also 680.24

Because essay performance for the examination candidate pool as a whole is scaled to the MBE distribution, rather than the reverse, there is a logical fallacy in extrapolating from a panel’s view of what a passing score might be for the essay portion (even assuming this were the product of a valid research protocol) to an overall passing grade for the examination. As the Board recognizes (Report at 15-16), whether candidates as a group perform well or poorly on the New York essays in comparison to standards that might be set by the Examiners or by an outside panel will not

24. Id. at 7-3 and 7-4 (passages combined and order reversed for clarity).
change the distribution of scaled scores and accordingly will not affect the passing rate. (Of course an individual candidate can affect his or her likelihood of achieving an overall passing score by better preparation or performance; the point being made here is about the scaling of the full pool’s results.)

We appreciate that this analysis of scaling may be both hard to follow and counter-intuitive. The Millman Evaluation acknowledged that the “procedures for arriving at the final examination scores are complicated and not understandable to many people.” Scaling to the same mean is used to “force” (i.e., impose) the assumption that each year’s NYMC, essays and MBE be regarded as equally difficult in terms of score (an assumption of equivalent rigor) so that higher scores on the essay in a particular year are assumed to be due to an “easier” test (warranting a scaling correction) rather than to an improvement in the candidate pool’s competence (which should be recognized, not obliterated by re-scaling).

In other words, if scores increase on the essays, thereby increasing the mean score on that part of the examination, scaling adjusts the essay scores because of the assumption that, to the extent the rise in essay scores was not accompanied by an equivalent rise in the mean MBE score, the increase in the mean essay score must indicate that the essay test has gotten easier, or the grading less rigorous. Scaling the essay scores to the MBE mean necessarily rejects the possibility that candidates have differentially improved their knowledge and skills applicable to the New York essays. Accordingly, the essay scores are deflated, so that the essay mean still matches the MBE mean. Conversely, if candidates as a group were to score higher on the MBE, thereby raising the mean MBE score, essay scores would be scaled higher even if there had been no true change in student performance on the essay portion of the test.

A study of essay performance might suggest that the essay section should be graded more or less rigorously than at present, but as long as the grades are scaled to the MBE distribution, uniformly applied changes in the rigor of essay grading should have no effect whatever on the scaled essay score. If the conclusion is that the norm for minimum competence with respect to performance on the essay portion should be adjusted “then the scaling process—not the passing score—should be reassessed” (Merritt Article at 937-38). Thus, Dr. Klein’s suggestion that further study by candidates could obviate the impact of the change in the passing score is misleading.

So long as there is scaling of essay raw scores to the MBE, then for the candidate pool as a whole only study aimed at improved MBE scores would be effective even though the panel’s work did not assess the sufficiency of performance on the MBE at all, having focused only on the quality of the essays.26

The assumption of equivalent rigor forced by scaling the other subtests to the MBE is not the only concern when proposing to reason from acceptable performance on the essay section to an overall pass/fail score. Dr. Klein’s extrapolation from essay performance to overall examination score depends on the further assumption that the essays and the MBE are measuring competence in a similar way for each year’s population of candidates, i.e., it depends on assuming that candidates are in general equally competent in each tested domain.

Dr. Klein’s method also requires the assumption that just-minimally competent candidates would achieve approximately the same score on the MBE and on the essay portion. We disagree. The mere fact that the tests are scaled to have the same mean score and standard deviation does not imply that equal scores on the different tests signify equal competence within the different knowledge/skill domains. Whether by reason of better preparation or otherwise, the competence rate in one domain may well be different from the competence rate in the other domains. Alternatively, experts might well conclude that the threshold measure of competence in one area differs from that in another. A particular score on MBE might signify insufficient competence while the same score on the essays might signify sufficient competence. Dr. Klein’s method requires that both the scale of competence and the threshold measure be at least approximately the same in all subtest domains in order to accurately apply the competence threshold set for the essay to the test as a whole. But the whole point of having multiple sections is the expectation that competent performance may very well differ across domains.

We have no doubt that there is some correlation between performance on the essays as a whole (measured by raw score) and performance on other portions of the test.27 However, the Board must believe that each section of the examination tests a distinct area of competence, in a distinct way—why else have so extensive an examination or use New York

26. The April 6, 2000, Comments of David M. White submitted to the Supreme Court of Florida in connection with its review of a similar study by Dr. Klein made this point: for the candidate pool as a whole, he commented, “improved essay writing will have no effect on the passing rate unless accompanied by improvement on the MBE.” (i.d. at.).

27. That was the case a decade ago. Millman Evaluation at 9-2 (showing relatively strong correlation).
essays in addition to an extensive multi-state multiple choice test? Multiple essay questions are used on bar examinations precisely to assess candidates' knowledge of different bodies of law, and for this reason the applicants' scores on different questions may show relatively low correlations (Merritt Article at 953-54). This means that it is reasonable to expect some applicants to score poorly on some questions and yet achieve a passing score on the exam as a whole. In this regard we again note that current Board policy is that there is no “passing” score for subparts of the examination, only for totality of performance.

We support a study of the essay portion of the New York exam that evaluates the essay section as a whole. Such a study might well support the conclusion that scores on the New York essays should be measured against some objective standard and directly added into the total score without scaling to the MBE distribution. This might result in a raising, or a lowering, of cohort scores. A study principally focused on the essays might even be able to conclude that the relative weighting of essays and MBE results should be changed. But even such a different study should not be the basis for changing the overall passing score, until and unless a great deal more was learned about the interplay of performance on the various segments of the examination.

3. The Need For Analysis Coupled With Standard Setting

To extrapolate from a standard-setting exercise to the overall passing score, the Board should conduct a thorough analysis of performance on the various segments of the examination, both before and after scaling. Such a study should be possible for the Board using data already available to it. The 1993 Millman Evaluation provides a framework for such a project as well as a baseline for determining to what extent, if any, there has been change in candidate performance over the last decade. We believe the Board should also study the fairly dramatic recent fluctuations in the passing rate on the examination.28 Such an analysis might make clear the extent to which such changes are a function of MBE performance rather than performance on the New York essays. They might also indicate whether because the essay score is scaled to the MBE, apparent declines in MBE performance are having a double effect by also artificially depressing scores for the New York essays independent of any objective change in the quality of essay responses.

28. Report at 16, footnote 21 states that the passing rate was 71.4% in July 1996, 67.5% in July 2000, and 72% in July 2001.
Setting a passing score—the line measuring “enough”—also requires analysis of the significance for the measurement of competence of the multiple choice questions (MBE and NYMC), weighted at 50% of total score. If the Board wants to review the usefulness of the overall passing score as a way to screen for minimum competence, it should review the entire test, using appropriate methods. That review should include a rethinking and testing of the various assumptions discussed above which underlie the current scoring system but remain essentially unstated and certainly unchallenged. Michael Kane has explained that procedures for assessing the use of multiple choice questions to measure competence are fundamentally different from procedures appropriate for assessing essay and performance tests.

Even assuming all reliability and validity issues were generally resolved in favor of the MBE (a topic far beyond the scope of this comment), the validity tests done for the MBE make no claim that MBE scores represent a linear scale of competence. The NCBE has not determined that any score on the MBE demonstrates “minimum competence.” Each state must make that determination for itself. If the Board is going to review the question of what essay performance demonstrates “minimum competence,” the MBE, which carries equivalent weight in the overall score, should be assessed as well. And surely the Board must be open to the possibility that performance on the MBE is over-weighted in the overall examination scoring.

4. Research Proposed By the Board

The Board proposes commissioning a study “to gather and assess de-
mographic information, including age, race and gender, and information regarding candidates' LSAT scores, law school GPA and quartile ranking, foreign education, and other information. The study will be used to study the correlation between demographic factors and other indicators and performance on the bar exam.” (Report at 14; the statement is repeated at 19.) We applaud that plan and would be eager to participate in the design of such a study. We differ with the Board, however, on the timing of such a study.

The Board proposes to embark on such a study only after increasing the passing score, “to study the impact of the increased score” (id.). The Board’s response is not what the public, the profession or the candidates should expect in such a “high stakes” situation. Given the potential impact of such a change, we believe such a study should be conducted to assist in deciding whether to increase the passing score.

Although the Board chastises those whose criticisms rest on “assumptions” about the current candidate pool (Report at 16), at this stage it is the Board that is assuming that a change in the passing score will produce a public benefit. If “standards for licensure are [to be] set by means of scientifically based studies informing our policy judgment,” the time to conduct those studies is before deciding to change the standard.

5. Timing of this Proposal and Studies By Others

The ABA, AALS, the National Conference of Bar Examiners, and the Conference of Chief Justices recently announced the formation of a Joint Working Group on Legal Education and Bar Admissions to study a number of far-ranging concerns related to the administration of the bar examination, including a “concern[] about the current trend toward increasing minimum bar examination passing scores and the methods that various states are using to establish those cut scores.”31 The Joint Working Group is planning to hold a nationwide conference in the winter of 2004 to address these and other concerns and also to consider a revision of the Code of Recommended Standards for Bar Examiners. Given the fact that the Joint Working Group has announced its intent to specifically study the process of setting a passing score in individual jurisdictions, we believe it would be prudent to delay the decision on any change in New York’s passing score until the work of that group is completed and fully evaluated.

31. Letter dated December 3, 2002 from John A. Sebert, Consultant on Legal Education to the American Bar Association to Professor Lawrence Grosberg, Chair, Committee on Legal Education and Admission to the Bar of the Association of the Bar of the City of New York.
CONCLUSION

We appreciate that the Board put substantial time, thought and effort into its Report, and we appreciate greatly the Board’s intention to have "scientifically based studies informing our policy judgments." In view of the objections and concerns we have discussed, however, we urge the Board to withdraw its proposal to raise the minimum passing score. Should the Board decide not to withdraw its recommendation, we respectfully urge the Court of Appeals to reject the recommendation. At the very least, we request that the Board defer its proposal pending further review, including both (i) completion of a study of the demographic data that will indicate whether and to what extent an increase in the passing score will affect both the diversity of the profession and consequent delivery of legal services to all sectors of the public, and (ii) the completion of other test-centered and competence-focused research discussed in this report.

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** Dissents