Monday, October 20
4:30 pm-6:00 pm

312 Managing Foreign Operations Under SOX and the FCPA

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Faculty Biographies

Katherine Choo

Katy Choo is senior counsel, litigation and legal policy, for General Electric and works from the company's Stamford, CT office. Ms. Choo focuses her practice on government and internal investigations (and related litigation), compliance issues in acquisitions, compliance initiatives of the company, and preventive law.

Prior to joining GE, Ms. Choo served as an assistant US attorney in the Southern District of New York for 11 years, where she worked as a deputy chief in the criminal division and as a chief of the general crimes unit. As an AUSA, Ms. Choo specialized in prosecutions of securities fraud and other white-collar offenses and was twice a recipient of the Justice Department's Director's Award for Superior Performance. Prior to her work as a federal prosecutor, Ms. Choo worked as a litigation associate at Davis Polk & Wardwell.

Ms. Choo received a BA from Wellesley College, where she was a Durant Scholar and a member of Phi Beta Kappa. Ms. Choo is also a graduate of Columbia School of Law, where she was a Harlan Fiske Stone Scholar.

Drew McKay

Drew McKay is executive vice president, general counsel, and secretary of the Fairfax Group, LLC in McLean, VA. He has been an executive in private consulting firms for 36 years, working for the Fairfax Group or its related companies.

Immediately prior to joining Fairfax, Mr. McKay was an assistant US Attorney for the District of Columbia. Mr. McKay also served in a variety of senior staff positions in the US Congress, including as staff director and general counsel of a joint committee. Mr. McKay served as the first assistant staff director for disclosure and compliance for the Federal Election Commission. While there, he administered the first public financing of a US Presidential election in 1976.

Mr. McKay is active in a number of professional associations, including the ACC where he has been chair of the national litigation committee, a member of the association foundation's board of directors, and a board member and president of the Metropolitan Washington, DC, Chapter.

Mr. McKay received a BA from Oakland University and is a graduate of the Washington College of Law at American University.

Catherine Muldoon

Catherine Muldoon is general counsel and chief global counsel for BDP International, Inc. (BDP) in Philadelphia. In this role, Ms. Muldoon is head of BDP's legal department with direct responsibility for all legal and contractual considerations associated with all mergers and acquisitions, joint ventures and business partners, tax planning, corporate structuring and strategy, business services, personnel, banking relations, and real estate. She is also responsible for managing litigation. Ms. Muldoon takes a lead role in corporate governance and risk management programs within BDP, ensuring that best practices are identified to the board of directors and implemented by the business units.

Prior to this position with BDP, Ms. Muldoon worked in private practice concentrating on commercial matters for corporate clients.

Ms. Muldoon earned a BA from The Johns Hopkins University and is a graduate of Seton Hall University School of Law.

Foreign Corrupt Practice Act

(Wink Wink, Nudge Nudge)

Creation of the FCPA

- Created in 1977 in response to global scandals
  - Watergate
  - Illegal payments by Lockheed to Japanese
  - Governments of France, Germany, Holland and Denmark allowed tax deductions for bribes as a cost of doing business.

Key Issues and Restrictions

- *Obeying export control laws*
  - *Export licenses*
- *Abstaining from boycotts*
  - *Businesses prohibited from participating in boycotts not sanctioned by US government*
- *Avoiding doing business with prohibited countries*
- *Adhering to FCPA*

Partner Convention

- Organization for Economic Cooperation and Development (OECD)
  - Antibribery Convention 1996
  - Ratified by the US in 1998 and added to the FCPA
  - Adopted by 31 global economies

To Whom does the FCPA apply?

- All US citizens, organizations, and employees operating internationally
- Regardless of where they are physically located
- Non-US companies and individuals if it occurred in the US.
- Non-US branches, subsidiaries, US owned companies incorporated in foreign countries.

Books and Records

- Corporation must keep detailed and accurate accounting records of ALL assets and transactions.
  - Cash
  - Bank accounts
  - Expenses may not be hidden or mischaracterized (slush fund)
  - SEC penalties would apply

So what is illegal?

- Three main areas of FCPA
  - Books and Records
  - Internal Controls
  - Anti bribery

Internal Controls

- Comply with all government regulations on:
  - Finance and accounting
  - Contract bidding procedures
  - Contractor selection procedures
  - Audit and internal authorizations processes
  - Enforced by SEC

Anti Bribery

- Prohibit authorizing to pay, or paying of anything of material value to a foreign official with the effort to obtain or retain business.
- OECD adds a provision prohibit bribes to gain an advantage
  - Payoff to extend a contract such as concession or production sharing
  - Anything that gives an unfair advantage
  - Gain a competitive edge through improper means

Promotional Expenses

- Promotional and business expenses are OK if they are reasonable and bona fide.
- SMALL gifts and gratuities
- Violations are determined by the purpose of the gift or gratuity.

Grease – OK to expedite a process

- Nominal sum made to secure or expedite what otherwise might be deemed routine government actions.
  - Processing paperwork (visas, work orders)
  - Police protection, mail, utilities, loading and unloading cargo.
- The difference is that you are not doing it to gain an advantage

Agents and Representatives

- Not a "Safe Harbor"
  - Cannot us an intermediary to carry out bribe
    - Pay a "commission" for expedite services
    - Money is used to bribe for an advantage
    - Vicarious liability for actions of agent
    - Should perform a background check on agent

Red Flags

- Using an agent with a reputation for bribing officials
- Agent's refusal to provide written confirmation they will abide by FCPA
- Agent's insistence their identity not be disclosed
- An agent's disclosed history of making bribes
- Suspicious requests. Being paid in cash, payment deposited in a foreign bank
- Agent requesting a commission far above the going rate.

Consequences

- Costly and embarrassing
  - Both the company AND the individual liable
  - Organization fines up to $2.5mm
  - Individual fines up to $1mm
  - Company cannot pay individual fines
  - 5-10+ years at the Graybar Hotel

Travel Expenses

- OK as long as they are bona fide and reasonable.
- Permissible to promote company products, services and executives.
- Must comply with local rules.

Foreign Corrupt Practices Act

Policy

I. Purpose

The purpose of this Policy is to ensure compliance by XXXXX Inc. ("XXX") and its directors, officers, employees, agents, consultants and representatives with the US Foreign Corrupt Practices Act ("FCPA") and related laws of other countries in which XXX does or intends to do business. XXX reserves the right to amend, rescind or replace this Policy at any time.

II. FCPA

2.1 Anti-Bribery

The FCPA is a US Federal Statute prohibiting US companies and their officers, directors, employees and agents from giving, promising or offering anything of value, whether directly or indirectly, to any foreign official (including an official of a public international organization) with the intention of obtaining or retaining business or obtaining an improper business advantage.

2.2 Record-Keeping and Internal Accounting Controls

The FCPA also requires US companies such as XXX to keep books and records that accurately reflect transactions and dispositions of assets and to maintain a system of internal accounting controls.

2.3 Penalties for Breach

Where the anti-bribery provisions of the FCPA are breached, the following penalties may be imposed:

(a) Fines of up to US$2 million against the company;

(b) Prison terms of up to five years and fines of up to US$100,000 per violation for individuals involved;

(c) The Securities and Exchange Commission ("SEC") may seek further civil penalties; and

(d) Where the record-keeping and accounting provisions of the FCPA are breached, SEC penalties for violation of securities laws may be invoked. Willful violations of the record-keeping provisions may result in up to 20 years imprisonment and US$5 million fines for individuals and up to US$25 million for companies.

III. Policy

3.1 Prohibition of Bribery of Foreign Official

Under no circumstance shall any XXX director, officer, employee, agent, consultant or representative (each of whom is covered herein by the term "XXX person") give, pay, offer, promise to pay, or authorise the giving or payment of money or other thing of value to any foreign official or to any person while knowing or being aware of a probability that the payment or promise to pay is being made to or will be passed on to a foreign official.

3.2 Prohibition of Payment or Gift in Violation of Local Law

Under no circumstance shall any XXX person make, offer, promise or authorize any payment or gift in violation of local law in any country.

3.3 Prohibition of Circumvention of Law

Under no circumstance shall any XXX person enter into any transaction that is intended or designed to circumvent the laws of any country. Any transaction that has the appearance of circumventing the laws of any country must be avoided.

3.4 Prohibition of Lawful Payment without Prior Approval

Under no circumstance shall any XXX person offer, pay, promise or give any money or other thing of value to any foreign official without the prior written approval of the President and Chief Executive Officer of XXX ("President"). While facilitating payments for routine, non-discretionary government functions are allowed by the FCPA, it is strict XXX policy that no such payment shall be made without the prior written approval of the President. Similarly, no political contribution or donation allowed by the FCPA shall be made by any XXX person without the prior written approval of the President.

3.5 Clarification of Uncertainty

Without prejudice to the foregoing requirement for written approval, an XXX person must promptly contact the President when questions arise concerning the FCPA's anti-bribery provisions including:

(a) Whether a particular individual or entity must be treated as a "foreign official";

(b) Whether something qualifies as anything of value; and

(c) Whether a proposed payment would be made or seen to be made to obtain, retain or direct business.

3.6 Due Diligence and Third-Party Certification

To avoid being held liable for corrupt third-party payments, XXX and any XXX person acting on its behalf must exercise due diligence at all times and take all necessary precautions to ensure that business relationships are formed only with reputable and qualified partners, agents and representatives. In negotiating any business relationship, it shall be recommended practice for XXX or any XXX person acting on XXX's behalf to require potential partners, agents or representatives to provide FCPA-compliance certification. Such certification shall include a covenant by the person providing it not to make or cause to be made any unlawful offer, promise, or payment to a foreign public official and not to do anything that would cause XXX to be in violation of the FCPA.

3.7 Record Keeping

All transactions involving XXX funds or assets should be recorded accurately and in reasonable detail. The record must completely reflect the transactions and asset dispositions of XXX wherever they take place.

3.8 Prohibition of Improper Accounting

Direct or indirect participation by any XXX person in any "improper transaction" or deviation from established XXX accounting practices, including omitted or falsified expense reports, is strictly prohibited.

3.9 Compulsory Compliance

Every XXX person shall comply with this Policy and be familiar with the Guidelines appended hereto. XXX may require XXX persons to undergo such FCPA compliance training or to obtain such FCPA compliance certifications as XXX may deem necessary from time to time.

3.10 Chief Compliance Officer

The President is the Chief Compliance Officer of XXX on FCPA matters. Any question regarding activities under consideration with regard to the FCPA or this Policy should be promptly directed to the President.

3.11 Sanction for Breach

This Policy is an integral part of XXX's Compliance Program. Any breach of this Policy by an XXX person may result in disciplinary action, termination, disengagement, civil proceedings, criminal prosecution or such other remedial or punitive action as shall be appropriate in the circumstances. Such action may be taken or initiated by XXX, governmental authority or other competent body. XXX will not directly or indirectly pay any fine imposed on any individual as a result of breach of the FCPA or of this Policy.

3.12 Zero Tolerance

XXX will not tolerate any XXX person that achieves or purports to achieve results for XXX in violation of law or by acting dishonestly. Conversely, XXX will fully support any XXX person who declines an opportunity or advantage, the securing of which would place XXX's ethical principles and reputation at risk.

IV. FCPA Background

The FCPA was originally enacted by the US Congress in 1977 and has been amended several times since. The FCPA is aimed at preventing corrupt practices by US business organisations doing or seeking business in foreign countries. In recent years, a number of large US companies involved in bribery in Nigeria, India, Venezuela, South Korea and elsewhere have been sanctioned by the US Government under the FCPA.
XXX is a publicly-traded US company registered with the US Securities and Exchange Commission ("SEC") and is covered by the provisions of the FCPA. XXX and its subsidiaries as well as every XXX person must therefore abide by the FCPA. Neither the complexity of the FCPA nor costs of compliance (including the loss of business) diminishes the responsibility to comply with the FCPA. It is imperative therefore that each and every XXX person becomes familiar with the FCPA's provisions.

V. Anti-Bribery and Keeping of Records

The FCPA has two parts. The anti-bribery part prohibits bribery of non-US public officials. The second part requires good record-keeping and internal accounting controls. The US Department of Justice ("DOJ") is responsible for the criminal enforcement of the anti-bribery provisions. The DOJ and the Securities and Exchange Commission ("SEC") share responsibility for administering civil penalties for breach of the anti-bribery provisions. SEC enforces the record-keeping and internal controls provisions.

VI. Anti-Bribery Provisions

6.1 Prohibition of Bribery of Foreign Officials

The FCPA prohibits XXX and any XXX person, whether acting in the United States or abroad, from giving or offering bribes to foreign officials in order to obtain or retain business, secure an improper advantage or direct business to any person. The business obtained or retained does not need to be with a foreign government or foreign

government instrumentality in order for the FCPA to apply.

6.2 Prohibited Conduct

For the avoidance of doubt, the elements of forbidden conduct under the anti-bribery provisions are as follows:

(a) Knowingly paying, offering, promising or authorizing to pay…

(b) Money or anything of value…

(c) Directly or indirectly…

(d) To any foreign official or political party…

(e) With the intention of influencing…

(f) The obtaining or retaining of business or otherwise securing any improper business advantage.

All of the elements must exist for the FCPA to have been breached. Each element is however explained separately, for purposes of clarity, in the following section.

V. Elements of FCPA Bribery

7.1 Knowingly Paying, Offering, Promising or Authorizing to Pay

The FCPA prohibits paying, offering, promising to pay (or authorizing to pay or offer) money or anything of value. A mere promise or offer of money or anything of value is sufficient to breach the FCPA, whether or not the promise was kept or offer fulfilled. Furthermore, the FCPA does not require that a forbidden act succeed in its purpose. The mere fact that the act was done, with or without achievement of its purpose, is a breach of the FCPA.

7.2 Money or Anything of Value

The use of the phrase “anything of value” means that the FCPA forbids not only money bribes but also bribes constituting such things as gifts, stock, entertainment, discounts on products and services not readily available to the public, offers of employment, assumption or forgiveness of debt, payment of travel expenses and personal favors.

7.3 Directly or Indirectly

The payment, offer or promise to pay does not have to be made directly by XXX or an XXX person. It is sufficient that it was made through an intermediary such as a broker, representative (including a stockholder when acting on behalf of XXX), joint-venture partner or subsidiary. It is also sufficient to breach the FCPA if the payment is made to an intermediary of a foreign official or foreign political party. Under the FCPA, it is unlawful to make a payment to a third party, while knowing that all or a portion of the payment will go directly or indirectly to a foreign official or a foreign political party. The term “knowing” here includes conscious disregard and deliberate ignorance.

7.4 Foreign Official or Foreign Political Party

The FCPA defines a “foreign official” as any officer or employee of a foreign government or any department, agency, or instrumentality of a foreign government. The term also includes any officer or employee of a public international organization such as the World Bank or the African Union. Furthermore, any person acting in an official capacity for any foreign-government agency, department or instrumentality, or for a public international organization is a ‘foreign official.’ An entity hired to review bids on behalf of a government agency would be covered by the term.

The DOJ has also stipulated that the following persons would be included in the definition of “foreign official”:

(a) Officers and employees of foreign state-owned companies;

(b) Uncompensated honorary officials if such officials can influence the awarding of business; and

(c) Members of royal families who have proprietary or managerial interests in industries and companies owned or controlled by the government.

The FCPA also prohibits bribes to foreign political parties and their officials as well as to candidates for foreign political office.

The FCPA applies to bribes or offers of bribes to the said officials, regardless of rank or position. The FCPA focuses on the purpose of the payment and not the duties or powers of the official receiving the payment, offer, or promise of payment.

7.5 Obtaining or retaining of business or otherwise securing any improper business advantage

The FCPA prohibits bribes or offers of bribes made in order to assist XXX in obtaining or retaining business for or with, or directing business to, any person. The DOJ interprets "obtaining or retaining business" broadly, to cover more than the mere award or renewal of a contract. For instance, payments made to reduce customs duties or other taxes are prohibited by the FCPA.

VIII. Permissible Payments and Affirmative Defenses

8.1 Exceptions to Anti-Bribery Provisions

The FCPA provides exceptions to the bribery prohibition. “Facilitating payments” made for “routine governmental action” do not constitute a breach of the FCPA. The FCPA also provides affirmative defenses against alleged violations of the FCPA.

8.2 Facilitating Payments for Routine Governmental Actions

The FCPA permits the payment of small sums to facilitate routine, non-discretionary government functions. However, each XXX person should always remember that under XXX’s FCPA Policy, facilitating payments cannot be made without the prior written approval of the XXX President and Chief Executive Officer (“President”).

The FCPA lists the following examples of routine governmental action:

(a) Issuance of permits, licenses, or other official documents;

(b) Processing governmental papers, such as visas and work permits providing police protection and mail pick-up and delivery;

(c) Providing phone service, power and water supply, loading and unloading cargo, or protecting perishable products; and

(d) Scheduling inspections associated with contract performance or transit of goods across country.

"Routine governmental action" does not include any decision by a foreign official to award new business or to continue business with a particular party.

8.3 Affirmative Defenses

It is a defense to a charge under the FCPA that the payment was lawful under the written laws of the foreign country or that the money was a bona fide, reasonable expense for the promotion of a product or performance of a contractual obligation. These are "affirmative defenses." It is the responsibility of any person that has made such payments to prove that the payments met the requirements for the defenses. Whether a payment was lawful under the written laws of a foreign country or is otherwise excused by the affirmative-defense provisions may be difficult to determine. It is for this reason that XXX’s FCPA Policy expressly prohibits payments to foreign officials without the prior written approval of the XXX President. The Policy intends thereby to ensure that all circumstances are properly considered before any payment is made.

IX. Penalties for Breach of Anti-Bribery Provisions

9.1 Criminal Penalties

The following criminal penalties may be imposed for violations of the FCPA's anti-bribery provisions:

(a) XXX may be fined up to US$2,000,000;

(b) Any XXX person found in violation is subject to a fine of up to US$100,000 and imprisonment for up to five years; and

(c) Under the Alternative Fines Act, higher fines may be imposed. The actual fine may be up to twice the benefit sought to be obtained by making the corrupt payment. It is forbidden for any fines imposed on an XXX person to be paid by XXX.

9.2 Civil Penalties

The Attorney General or SEC, as the case may be, may bring civil proceedings for a fine of up to $10,000 against XXX and any XXX person who violates the anti-bribery provisions. In a SEC enforcement action, the court may impose an additional fine not to exceed the greater of (i) the gross amount of the pecuniary gain to the defendant as a result of the violation, or (ii) a specified dollar limitation. The specified dollar limitation depends on the seriousness of the violation and will range from $5,000 to $100,000 for a natural person and $50,000 to $500,000 for any other person.

The Attorney General or SEC, as the case may be, may also bring a civil action to enjoin any activity of XXX or an XXX person which is violating or about to violate the anti-bribery provisions.

9.3 Other Governmental Action

The Office of Management and Budget (“OMB”) has guidelines under which any person or entity found in violation of the FCPA may be barred from doing business with the Federal government. The mere fact of indictment can lead to suspension of the right to do business with the US government.

In addition, a person or firm found guilty of violating the FCPA may be declared ineligible for export licenses. SEC may suspend or bar persons in violation of the FCPA from the securities business and impose civil penalties. The Commodity Futures Trading Commission and the Overseas Private Investment Corporation may impose suspension or debarment from agency programs for violation of the FCPA. Any payment that violates the FCPA cannot be deducted as a business expense for tax purposes.

9.4 Private Cause of Action

Violating the FCPA may also form the basis for a private cause of action for treble damages under the Racketeer Influenced and Corrupt Organizations Act ("RICO"). It may also give rise to actions under other federal or state laws. For example, a competitor may bring an action under RICO on the ground that the defendant won foreign contract under RICO.

X. Internal Accounting Controls and Record Keeping

10.1 Maintenance of Books and Controls

Apart from the compliance with its anti-bribery provisions, the FCPA requires XXX to abide by the provisions of the Act that require:

(a) Maintenance of books and records which in reasonable detail, accurately and fairly reflect each transaction and disposition of XXX assets; and

(b) Maintenance of a system of internal accounting controls sufficient to provide reasonable assurances that, among other things, transactions have been executed in accordance with management's specific authorization and recorded in accordance with generally accepted accounting principles ("GAAP").

10.2 Criminal Offence in Breach

It is a criminal offence for any person to knowingly circumvent or fail to maintain a system of internal accounting controls. It is also a crime to knowingly falsify any books or records pertaining to XXX transactions. These provisions are intended to discourage fraudulent accounting practices and to prevent the concealment of bribes to foreign public officials.

10.3 Responsibility for Subsidiaries

Under the FCPA, XXX is responsible for ensuring that its wholly owned subsidiaries comply with the provisions. Where XXX owns less 50% of less of the voting power of a subsidiary, XXX must in good faith use its influence to the extent reasonable in the circumstances to cause the subsidiary to maintain proper records and accounting control.

10.4 Reasonable Detail and Assurance

"Reasonable detail" and "reasonable assurance" mean such level of detail and degree of assurance as would satisfy prudent officials in the conduct of their own business.

10.5 Penalties for Breach

Breach of the recordkeeping and accounting provisions of the FCPA are currently punishable as follows:

(a) Imprisonment of up to 20 years and fines of up to US$25 million for individuals; and

(b) Fines of up to US$25 million for companies.

The Sarbanes-Oxley Act ("SOX") also provides fines and up to 20 years imprisonment for certain acts connected with recordkeeping failures. SOX prohibits criminally altering, destroying or concealing any record with intent to obstruct the investigation or administration of any matter within the jurisdiction of the US government.

Adoption by the Board of XXX

The forgoing FCPA Policy was adopted by the Board of Directors of XXXXX Inc. on the ___ day of _____ 2008.

This FCPA Policy is not represented to be an exhaustive explanation of all the specific provisions or intricacies of the FCPA. The full text of the Act is available on the website of the US Department of Justice at www.usdoj.gov/criminal/fraud/fcpa/fcpastat.htm. Any questions regarding the applicability or effect of the FCPA with regard to any transaction or activity by XXX or by any XXX person on behalf of XXX should be directed to XXX's President and Chief Executive Officer ("President"). It should however be borne in mind at all times that each XXX person has direct, personal responsibility for complying with the FCPA. Each XXX person may therefore wish to seek guidance from his or her own counsel as well.

Provisions of The Foreign Corrupt Practices Act
Current through Pub. L. 105-366 (November 10, 1998)
UNITED STATES CODE TITLE 15.
COMMERCE AND TRADE CHAPTER 2B--SECURITIES EXCHANGES

§ 78m. Periodical and other reports

(a) Reports by issuer of security; contents

Every issuer of a security registered pursuant to section 78l of this title shall file with the Commission, in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate for the proper protection of investors and to insure fair dealing in the security--

(1) such information and documents (and such copies thereof) as the Commission shall require to keep reasonably current the information and documents required to be included in or filed with an application or registration statement filed pursuant to section 78l of this title, except that the Commission may not require the filing of any material contract wholly executed before July 1, 1962.

(2) such annual reports (and such copies thereof), certified if required by the rules and regulations of the Commission by independent public accountants, and such quarterly reports (and such copies thereof), as the Commission may prescribe.

Every issuer of a security registered on a national securities exchange shall also file a duplicate original of such information, documents, and reports with the exchange.

(b) Form of report; books, records, and internal accounting; directives

* * *

(2) Every issuer which has a class of securities registered pursuant to section 78l of this title and every issuer which is required to file reports pursuant to section 78o(d) of this title shall--

(A) make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer; and

(B) devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that--

(i) transactions are executed in accordance with management's general or specific authorization;

(ii) transactions are recorded as necessary (I) to permit preparation of financial statements in conformity with generally accepted accounting principles or any other criteria applicable to such statements, and (II) to maintain accountability for assets;

(iii) access to assets is permitted only in accordance with management's general or specific authorization; and

(iv) the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences.

(3) (A) With respect to matters concerning the national security of the United States, no duty or liability under paragraph (2) of this subsection shall be imposed upon any person acting in cooperation with the head of any Federal department or agency responsible for such matters if such act in cooperation with such head of a department or agency was done upon the specific, written directive of the head of such department or agency pursuant to Presidential authority to issue such directives. Each directive issued under this paragraph shall set forth the specific facts and circumstances with respect to which the provisions of this paragraph are to be invoked. Each such directive shall, unless renewed in writing, expire one year after the date of issuance.
(B) Each head of a Federal department or agency of the United States who issues such a directive pursuant to this paragraph shall maintain a complete file of all such directives and shall, on October 1 of each year, transmit a summary of matters covered by such directives in force at any time during the previous year to the Permanent Select Committee on Intelligence of the House of Representatives and the Select Committee on Intelligence of the Senate.

(4) No criminal liability shall be imposed for failing to comply with the requirements of paragraph (2) of this subsection except as provided in paragraph (5) of this subsection.

(5) No person shall knowingly circumvent or knowingly fail to implement a system of internal accounting controls or knowingly falsify any book, record, or account described in paragraph (2).

(6) Where an issuer which has a class of securities registered pursuant to section 78l of this title or an issuer which is required to file reports pursuant to section 78o(d) of this title holds 50 per centum or less of the voting power with respect to a domestic or foreign firm, the provisions of paragraph (2) require only that the issuer proceed in good faith to use its influence, to the extent reasonable under the issuer's circumstances, to cause such domestic or foreign firm to devise and maintain a system of internal accounting controls consistent with paragraph (2). Such circumstances include the relative degree of the issuer's ownership of the domestic or foreign firm and the laws and practices governing the business operations of the country in which such firm is located. An issuer which demonstrates good faith efforts to use such influence shall be conclusively presumed to have complied with the requirements of paragraph (2).

(7) For the purpose of paragraph (2) of this subsection, the terms "reasonable assurances" and "reasonable detail" mean such level of detail and degree of assurance as would satisfy prudent officials in the conduct of their own affairs.

* * *

§ 78dd-1 [Section 30A of the Securities & Exchange Act of 1934].

Prohibited foreign trade practices by issuers

(a) Prohibition

It shall be unlawful for any issuer which has a class of securities registered pursuant to section 78l of this title or which is required to file reports under section 78o(d) of this title, or for any officer, director, employee, or agent of such issuer or any stockholder thereof acting on behalf of such issuer, to make use of the mails or any means or instrumentality of interstate commerce corruptly in furtherance of an offer, payment, promise to pay, or authorization of the payment of any money, or offer, gift, promise to give, or authorization of the giving of anything of value to--

(1) any foreign official for purposes of--

(A) (i) influencing any act or decision of such foreign official in his official capacity, (ii) inducing such foreign official to do or omit to do any act in violation of the lawful duty of such official, or (iii) securing any improper advantage; or

(B) inducing such foreign official to use his influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality,

in order to assist such issuer in obtaining or retaining business for or with, or directing business to, any person;

(2) any foreign political party or official thereof or any candidate for foreign political office for purposes of--

(A) (i) influencing any act or decision of such party, official, or candidate in its or his official capacity, (ii) inducing such party, official, or candidate to do or omit to do an act in violation of the lawful duty of such party, official, or candidate, or (iii) securing any improper advantage; or

(B) inducing such party, official, or candidate to use its or his influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality.

in order to assist such issuer in obtaining or retaining business for or with, or directing business to, any person; or

(3) any person, while knowing that all or a portion of such money or thing of value will be offered, given, or promised, directly or indirectly, to any foreign official, to any foreign political party or official thereof, or to any candidate for foreign political office, for purposes of--

(A) (i) influencing any act or decision of such foreign official, political party, party official, or candidate in his or its official capacity, (ii) inducing such foreign official, political party, party official, or candidate to do or omit to do any act in violation of the lawful duty of such foreign official, political party, party official, or candidate, or (iii) securing any improper advantage; or

(B) inducing such foreign official, political party, party official, or candidate to use his or its influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality,

in order to assist such issuer in obtaining or retaining business for or with, or directing business to, any person.

(b) Exception for routine governmental action

Subsections (a) and (g) of this section shall not apply to any facilitating or expediting payment to a foreign official, political party, or party official the purpose of which is to expedite or to secure the performance of a routine governmental action by a foreign official, political party, or party official.

(c) Affirmative defenses

It shall be an affirmative defense to actions under subsection (a) or (g) of this section that--

(1) the payment, gift, offer, or promise of anything of value that was made, was lawful under the written laws and regulations of the foreign official's, political party's, party official's, or candidate's country; or

(2) the payment, gift, offer, or promise of anything of value that was made, was a reasonable and bona fide expenditure, such as travel and lodging expenses, incurred by or on behalf of a foreign official, party, party official, or candidate and was directly related to--

(A) the promotion, demonstration, or explanation of products or services; or

(B) the execution or performance of a contract with a foreign government or agency thereof.

(d) Guidelines by Attorney General

Not later than one year after August 23, 1988, the Attorney General, after consultation with the Commission, the Secretary of Commerce, the United States Trade Representative, the Secretary of State, and the Secretary of the Treasury, and after obtaining the views of all interested persons through public notice and comment procedures, shall determine to what extent compliance with this section would be enhanced and the business community would be assisted by further clarification of the preceding provisions of this section and may, based on such determination and to the extent necessary and appropriate, issue--

(1) guidelines describing specific types of conduct, associated with common types of export sales arrangements and business contracts, which for purposes of the Department of Justice's present enforcement policy, the Attorney General determines would be in conformance with the preceding provisions of this section; and

(2) general precautionary procedures which issuers may use on a voluntary basis to conform their conduct to the Department of Justice's present enforcement policy regarding the preceding provisions of this section.

The Attorney General shall issue the guidelines and procedures referred to in the preceding sentence in accordance with the provisions of subchapter II of chapter 5 of Title 5 and those guidelines and procedures shall be subject to the provisions of chapter 7 of that title.

(e) Opinions of Attorney General

(1) The Attorney General, after consultation with appropriate departments and agencies of the United States and after obtaining the views of all interested persons through public notice and comment procedures, shall establish a procedure to provide responses to specific inquiries by issuers concerning conformance of their conduct with the Department of Justice's present enforcement policy regarding the preceding provisions of this section. The Attorney General shall, within 30 days after receiving such a request, issue an opinion in response to that request. The opinion shall state whether or not certain specified prospective conduct would, for purposes of the Department of Justice's present enforcement policy, violate the preceding provisions of this section. Additional requests for opinions may be filed with the Attorney General regarding other specified prospective conduct that is beyond the scope of conduct specified in previous requests. In any action brought under the applicable provisions of this section, there shall be a rebuttable presumption that conduct, which is specified in a request by an issuer and for which the Attorney General has issued an opinion that such conduct is in conformity with the Department of Justice's present enforcement policy, is in compliance with the preceding provisions of this section. Such a presumption may be rebutted by a preponderance of the evidence. In considering the presumption for purposes of this paragraph, a court shall weight all relevant factors, including but not limited to whether the information submitted to the Attorney General was accurate and complete and whether it was within the scope of the conduct specified in any request received by the Attorney General. The Attorney General shall establish the procedure required by this paragraph in accordance with the provisions of subchapter II of chapter 5 of Title 5 and that procedure shall be subject to the provisions of chapter 7 of that title.

(2) Any document or other material which is provided to, received by, or prepared in the Department of Justice or any other department or agency of the United States in connection with a request by an issuer under the procedure established under paragraph (1), shall be exempt from disclosure under section 552 of Title 5 and shall not, except with the consent of the issuer,

be made publicly available, regardless of whether the Attorney General responds to such a request or the issuer withdraws such request before receiving a response.

(3) Any issuer who has made a request to the Attorney General under paragraph (1) may withdraw such request prior to the time the Attorney General issues an opinion in response to such request. Any request so withdrawn shall have no force or effect.

(4) The Attorney General shall, to the maximum extent practicable, provide timely guidance concerning the Department of Justice's present enforcement policy with respect to the preceding provisions of this section to potential exporters and small businesses that are unable to obtain specialized counsel on issues pertaining to such provisions. Such guidance shall be limited to responses to requests under paragraph (1) concerning conformity of specified prospective conduct with the Department of Justice's present enforcement policy regarding the preceding provisions of this section and general explanations of compliance responsibilities and of potential liabilities under the preceding provisions of this section.

(f) Definitions

For purposes of this section:

(1) A) The term "foreign official" means any officer or employee of a foreign government or any department, agency, or instrumentality thereof, or of a public international organization, or any person acting in an official capacity for or on behalf of any such government or department, agency, or instrumentality, or for or on behalf of any such public international organization.
(B) For purposes of subparagraph (A), the term "public international organization" means--
(i) an organization that is designated by Executive Order pursuant to section 1 of the International Organizations Immunities Act (22 U.S.C. § 288); or
(ii) any other international organization that is designated by the President by Executive order for the purposes of this section, effective as of the date of publication of such order in the Federal Register.

(2) (A) A person's state of mind is "knowing" with respect to conduct, a circumstance, or a result if--
(i) such person is aware that such person is engaging in such conduct, that such circumstance exists, or that such result is substantially certain to occur; or
such person has a firm belief that such circumstance exists or that such
(ii) result is substantially certain to occur.

(B) When knowledge of the existence of a particular circumstance is required for an offense, such knowledge is established if a person is aware of a high probability of the existence of such circumstance, unless the person actually believes that such circumstance does not exist.

(3) (A) The term "routine governmental action" means only an action which is ordinarily and commonly performed by a foreign official in--
(i) obtaining permits, licenses, or other official documents to qualify a person to do business in a foreign country;

(ii) processing governmental papers, such as visas and work orders;

(iii) providing police protection, mail pick-up and delivery, or scheduling inspections associated with contract performance or inspections related to transit of goods across country;

(iv) providing phone service, power and water supply, loading and unloading cargo, or protecting perishable products or commodities from deterioration; or

(v) actions of a similar nature.

(B) The term "routine governmental action" does not include any decision by a foreign official whether, or on what terms, to award new business to or to continue business with a particular party, or any action taken by a foreign official involved in the decision-making process to encourage a decision to award new business to or continue business with a particular party.

(g) Alternative Jurisdiction

(1) It shall also be unlawful for any issuer organized under the laws of the United States, or a State, territory, possession, or commonwealth of the United States or a political subdivision thereof and which has a class of securities registered pursuant to section 12 of this title or which is required to file reports under section 15(d) of this title, or for any United States person that is an officer, director, employee, or agent of such issuer or a stockholder thereof acting on behalf of such issuer, to corruptly do any act outside the United States in furtherance of an offer, payment, promise to pay, or authorization of the payment of any money, or offer, gift, promise to give, or authorization of the giving of anything of value to any of the persons or entities set forth in paragraphs (1), (2), and (3) of this subsection (a) of this section for the purposes set forth therein, irrespective of whether such issuer or such officer, director, employee, agent, or stockholder makes use of the mails or any means or instrumentality of interstate commerce in furtherance of such offer, gift, payment, promise, or authorization.

(2) As used in this subsection, the term "United States person" means a national of the United States (as defined in section 101 of the Immigration and Nationality Act (8 U.S.C. § 1101)) or any corporation, partnership, association, joint-stock company, business trust, unincorporated organization, or sole proprietorship organized under the laws of the United States or any State, territory, possession, or commonwealth of the United States, or any political subdivision thereof.

§ 78dd-2. Prohibited foreign trade practices by domestic concerns

(a) Prohibition

It shall be unlawful for any domestic concern, other than an issuer which is subject to section 78dd-1 of this title, or for any officer, director, employee, or agent of such domestic concern or any stockholder thereof acting on behalf of such domestic concern, to make use of the mails or any means or instrumentality of interstate commerce corruptly in furtherance of an offer, payment, promise to pay, or authorization of the payment of any money, or offer, gift, promise to give, or authorization of the giving of anything of value to--

(1) any foreign official for purposes of--

(A) (i) influencing any act or decision of such foreign official in his official capacity, (ii) inducing such foreign official to do or omit to do any act in violation of the lawful duty of such official, or (iii) securing any improper advantage; or

(B) inducing such foreign official to use his influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality,

in order to assist such domestic concern in obtaining or retaining business for or with, or directing business to, any person;

(2) any foreign political party or official thereof or any candidate for foreign political office for purposes of--

(A) (i) influencing any act or decision of such party, official, or candidate in its or his official capacity, (ii) inducing such party, official, or candidate to do or omit to do an act in violation of the lawful duty of such party, official, or candidate, or (iii) securing any improper advantage; or

(B) inducing such party, official, or candidate to use its or his influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality,

in order to assist such domestic concern in obtaining or retaining business for or with, or directing business to, any person;

(3) any person, while knowing that all or a portion of such money or thing of value will be offered, given, or promised, directly or indirectly, to any foreign official, to any foreign political party or official thereof, or to any candidate for foreign political office, for purposes of--

(A) (i) influencing any act or decision of such foreign official, political party, party official, or candidate in his or its official capacity, (ii) inducing such foreign official, political party, party official, or candidate to do or omit to do any act in violation of the lawful duty of such foreign official, political party, party official, or candidate, or (iii) securing any improper advantage; or

(B) inducing such foreign official, political party, party official, or candidate to use his or its influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality,

in order to assist such domestic concern in obtaining or retaining business for or with, or directing business to, any person.

(b) Exception for routine governmental action

Subsections (a) and (i) of this section shall not apply to any facilitating or expediting payment to a foreign official, political party, or party official the purpose of which is to expedite or to secure the performance of a routine governmental action by a foreign official, political party, or party official.

(c) Affirmative defenses

It shall be an affirmative defense to actions under subsection (a) or (i) of this section that--

(1) the payment, gift, offer, or promise of anything of value that was made, was lawful under the written laws and regulations of the foreign official's, political party's, party official's, or candidate's country; or

(2) the payment, gift, offer, or promise of anything of value that was made, was a reasonable and bona fide expenditure, such as travel and lodging expenses, incurred by or on behalf of a foreign official, party, party official, or candidate and was directly related to--

(A) the promotion, demonstration, or explanation of products or services; or

(B) the execution or performance of a contract with a foreign government or agency thereof.

(d) Injunctive relief

(1) When it appears to the Attorney General that any domestic concern to which this section applies, or officer, director, employee, agent, or stockholder thereof, is engaged, or about to engage, in any act or practice constituting a violation of subsection (a) or (i) of this section, the Attorney General may, in his discretion, bring a civil action in an appropriate district court of the United States to enjoin such act or practice, and upon a proper showing, a permanent injunction or a temporary restraining order shall be granted without bond.

(2) For the purpose of any civil investigation which, in the opinion of the Attorney General, is necessary and proper to enforce this section, the Attorney General or his designee are empowered to administer oaths and affirmations, subpoena witnesses, take evidence, and require the production of any books, papers, or other documents which the Attorney General deems relevant or material to such investigation. The attendance of witnesses and the production of documentary evidence may be required from any place in the United States, or any territory, possession, or commonwealth of the United States, at any designated place of hearing.

(3) In case of contumacy by, or refusal to obey a subpoena issued to, any person, the Attorney General may invoke the aid of any court of the United States within the jurisdiction of which such investigation or proceeding is carried on, or where such person resides or carries on business, in requiring the attendance and testimony of witnesses and the production of books, papers, or other documents. Any such court may issue an order requiring such person to appear before the Attorney General or his designee, there to produce records, if so ordered, or to give testimony touching the matter under investigation. Any failure to obey such order of the court may be punished by such court as a contempt thereof.

All process in any such case may be served in the judicial district in which such person resides or may be found. The Attorney General may make such rules relating to civil investigations as may be necessary or appropriate to implement the provisions of this subsection.

(e) Guidelines by Attorney General

Not later than 6 months after August 23, 1988, the Attorney General, after consultation with the Securities and Exchange Commission, the Secretary of Commerce, the United States Trade Representative, the Secretary of State, and the Secretary of the Treasury, and after obtaining the views of all interested persons through public notice and comment procedures, shall determine to what extent compliance with this section would be enhanced and the business community would be assisted by further clarification of the preceding provisions of this section and may, based on such determination and to the extent necessary and appropriate, issue--

(1) guidelines describing specific types of conduct, associated with common types of export sales arrangements and business contracts, which for purposes of the Department of Justice's present enforcement policy, the Attorney General determines would be in conformance with the preceding provisions of this section; and

(2) general precautionary procedures which domestic concerns may use on a voluntary basis to conform their conduct to the Department of Justice's present enforcement policy regarding the preceding provisions of this section.

The Attorney General shall issue the guidelines and procedures referred to in the preceding sentence in accordance with the provisions of subchapter II of chapter 5 of Title 5 and those guidelines and procedures shall be subject to the provisions of chapter 7 of that title.

(f) Opinions of Attorney General

(1) The Attorney General, after consultation with appropriate departments and agencies of the United States and after obtaining the views of all interested persons through public notice and comment procedures, shall establish a procedure to provide responses to specific inquiries by domestic concerns concerning conformance of their conduct with the Department of Justice's present enforcement policy regarding the preceding provisions of this section. The Attorney General shall, within 30 days after receiving such a request, issue an opinion in response to that

request. The opinion shall state whether or not certain specified prospective conduct would, for purposes of the Department of Justice's present enforcement policy, violate the preceding provisions of this section. Additional requests for opinions may be filed with the Attorney General regarding other specified prospective conduct that is beyond the scope of conduct specified in previous requests. In any action brought under the applicable provisions of this section, there shall be a rebuttable presumption that conduct, which is specified in a request by a domestic concern and for which the Attorney General has issued an opinion that such conduct is in conformity with the Department of Justice's present enforcement policy, is in compliance with the preceding provisions of this section. Such a presumption may be rebutted by a preponderance of the evidence. In considering the presumption for purposes of this paragraph, a court shall weigh all relevant factors, including but not limited to whether the information submitted to the Attorney General was accurate and complete and whether it was within the scope of the conduct specified in any request received by the Attorney General. The Attorney General shall establish the procedure required by this paragraph in accordance with the provisions of subchapter II of chapter 5 of Title 5 and that procedure shall be subject to the provisions of chapter 7 of that title.

(2) Any document or other material which is provided to, received by, or prepared in the Department of Justice or any other department or agency of the United States in connection with a request by a domestic concern under the procedure established under paragraph (1), shall be exempt from disclosure under section 552 of Title 5 and shall not, except with the consent of the domestic concern, by made publicly available, regardless of whether the Attorney General response to such a request or the domestic concern withdraws such request before receiving a response.

(3) Any domestic concern who has made a request to the Attorney General under paragraph (1) may withdraw such request prior to the time the Attorney General issues an opinion in response to such request. Any request so withdrawn shall have no force or effect.

(4) The Attorney General shall, to the maximum extent practicable, provide timely guidance concerning the Department of Justice's present enforcement policy with respect to the preceding provisions of this section to potential exporters and small businesses that are unable to obtain specialized counsel on issues pertaining to such provisions. Such guidance shall be limited to responses to requests under paragraph (1) concerning conformity of specified prospective conduct with the Department of Justice's present enforcement policy regarding the preceding provisions of this section and general explanations of compliance responsibilities and of potential liabilities under the preceding provisions of this section.

(g) Penalties

(1) (A) Any domestic concern that is not a natural person and that violates subsection (a) or (i) of this section shall be fined not more than $2,000,000.

(B) Any domestic concern that is not a natural person and that violates subsection (a) or (i) of this section shall be subject to a civil penalty of not more than $10,000 imposed in an action brought by the Attorney General.

(2) (A) Any natural person that is an officer, director, employee, or agent of a domestic concern, or stockholder acting on behalf of such domestic concern, who willfully violates subsection (a) or (i) of this section shall be fined not more than $100,000 or imprisoned not more than 5 years, or both.

(B) Any natural person that is an officer, director, employee, or agent of a domestic concern, or stockholder acting on behalf of such domestic concern, who violates subsection (a) or (i) of this section shall be subject to a civil penalty of not more than $10,000 imposed in an action brought by the Attorney General.

(3) Whenever a fine is imposed under paragraph (2) upon any officer, director, employee, agent, or stockholder of a domestic concern, such fine may not be paid, directly or indirectly, by such domestic concern.

(h) Definitions

For purposes of this section:

(1) The term "domestic concern" means--
(A) any individual who is a citizen, national, or resident of the United States; and

(B) any corporation, partnership, association, joint-stock company, business trust, unincorporated organization, or sole proprietorship which has its principal place of business in the United States, or which is organized under the laws of a State of the United States or a territory, possession, or commonwealth of the United States.

(2) (A) The term "foreign official" means any officer or employee of a foreign government or any department, agency, or instrumentality thereof, or of a public international organization, or any person acting in an official capacity for or on behalf of any such government or department, agency, or instrumentality, or for or on behalf of any such public international organization.

(B) For purposes of subparagraph (A), the term "public international organization" means --

(i) an organization that has been designated by Executive order pursuant to Section 1 of the International Organizations Immunities Act (22 U.S.C. § 288); or

(ii)any other international organization that is designated by the President by Executive order for the purposes of this section, effective as of the date of publication of such order in the Federal Register.

(3) (A) A person's state of mind is "knowing" with respect to conduct, a circumstance, or a result if--
(i) such person is aware that such person is engaging in such conduct, that such circumstance exists, or that such result is substantially certain to occur; or

(ii) such person has a firm belief that such circumstance exists or that such result is substantially certain to occur.

(B) When knowledge of the existence of a particular circumstance is required for an offense, such knowledge is established if a person is aware of a high probability of the existence of such circumstance, unless the person actually believes that such circumstance does not exist.

(4) (A) The term "routine governmental action"means only an action which is ordinarily and commonly performed by a foreign official in--
(i) obtaining permits, licenses, or other official documents to qualify a person to do business in a foreign country;

(ii) processing governmental papers, such as visas and work orders;

(iii) providing police protection, mail pick-up and delivery, or scheduling inspections associated with contract performance or inspections related to transit of goods across country;

(iv) providing phone service, power and water supply, loading and unloading cargo, or protecting perishable products or commodities from deterioration; or

(v) actions of a similar nature.

(B) The term "routine governmental action" does not include any decision by a foreign official whether, or on what terms, to award new business to or to continue business with a particular party, or any action taken by a foreign official involved in the decision-making process to encourage a decision to award new business to or continue business with a particular party.

(5) The term "interstate commerce"means trade, commerce, transportation, or communication among the several States, or between any foreign country and any State or between any State and any place or ship outside thereof, and such term includes the intrastate use of--

(A) a telephone or other interstate means of communication, or

(B) any other interstate instrumentality.

(i) Alternative Jurisdiction

(1) It shall also be unlawful for any United States person to corruptly do any act outside the United States in furtherance of an offer, payment, promise to pay, or authorization of the payment of any money, or offer, gift, promise to give, or authorization of the giving of anything of value to any of the persons or entities set forth in paragraphs (1), (2), and (3) of subsection (a), for the purposes set forth therein, irrespective of whether such United States person makes use of the mails or any means or instrumentality of interstate commerce in furtherance of such offer, gift, payment, promise, or authorization.
(2) As used in this subsection, a "United States person"means a national of the United States (as defined in section 101 of the Immigration and Nationality Act (8 U.S.C. § 1101)) or any corporation, partnership, association, joint-stock company, business trust, unincorporated organization, or sole proprietorship organized under the laws of the United States or any State, territory, possession, or commonwealth of the United States, or any political subdivision thereof.

§ 78dd-3. Prohibited foreign trade practices by persons other than issuers or domestic concerns

(a) Prohibition

It shall be unlawful for any person other than an issuer that is subject to section 30A of the Securities Exchange Act of 1934 or a domestic concern, as defined in section 104 of this Act), or for any officer, director, employee, or agent of such person or any stockholder thereof acting on behalf of such person, while in the territory of the United States, corruptly to make use of the mails or any means or instrumentality of interstate commerce or to do any other act in furtherance of an offer, payment, promise to pay, or authorization of the payment of any money, or offer, gift, promise to give, or authorization of the giving of anything of value to--

(1) any foreign official for purposes of--

(A) (i) influencing any act or decision of such foreign official in his official capacity, (ii) inducing such foreign official to do or omit to do any act in violation of the lawful duty of such official, or (iii) securing any improper advantage; or

(B) inducing such foreign official to use his influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality,

in order to assist such person in obtaining or retaining business for or with, or directing business to, any person;

(2) any foreign political party or official thereof or any candidate for foreign political office for purposes of--

(A) (i) influencing any act or decision of such party, official, or candidate in its or his official capacity, (ii) inducing such party, official, or candidate to do or omit to do an act in violation of the lawful duty of such party, official, or candidate, or (iii) securing any improper advantage; or

(B) inducing such party, official, or candidate to use its or his influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality.

in order to assist such person in obtaining or retaining business for or with, or directing business to, any person; or

(3) any person, while knowing that all or a portion of such money or thing of value will be offered, given, or promised, directly or indirectly, to any foreign official, to any foreign political party or official thereof, or to any candidate for foreign political office, for purposes of--

(A) (i) influencing any act or decision of such foreign official, political party, party official, or candidate in his or its official capacity, (ii) inducing such foreign official, political party, party official, or candidate to do or omit to do any act in violation of the lawful duty of such foreign official, political party, party official, or candidate, or (iii) securing any improper advantage; or

(B) inducing such foreign official, political party, party official, or candidate to use his or its influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality,

in order to assist such person in obtaining or retaining business for or with, or directing business to, any person.

(b) Exception for routine governmental action

Subsection (a) of this section shall not apply to any facilitating or expediting payment to a foreign official, political party, or party official the purpose of which is to expedite or to secure the performance of a routine governmental action by a foreign official, political party, or party official.

(c) Affirmative defenses

It shall be an affirmative defense to actions under subsection (a) of this section that--

(1) the payment, gift, offer, or promise of anything of value that was made, was lawful under the written laws and regulations of the foreign official's, political party's, party official's, or candidate's country; or

(2) the payment, gift, offer, or promise of anything of value that was made, was a reasonable and bona fide expenditure, such as travel and lodging expenses, incurred by or on behalf of a foreign official, party, party official, or candidate and was directly related to--

(A) the promotion, demonstration, or explanation of products or services; or

(B) the execution or performance of a contract with a foreign government or agency thereof.

(d) Injunctive relief

(1) When it appears to the Attorney General that any person to which this section applies, or officer, director, employee, agent, or stockholder thereof, is engaged, or about to engage, in any act or practice constituting a violation of subsection (a) of this section, the Attorney General may, in his discretion, bring a civil action in an appropriate district court of the United States to enjoin such act or practice, and upon a proper showing, a permanent injunction or a temporary restraining order shall be granted without bond.

(2) For the purpose of any civil investigation which, in the opinion of the Attorney General, is necessary and proper to enforce this section, the Attorney General or his designee are empowered to administer oaths and affirmations, subpoena witnesses, take evidence, and require the production of any books, papers, or other documents which the Attorney General deems relevant or material to such investigation. The attendance of witnesses and the production of documentary evidence may be required from any place in the United States, or any territory, possession, or commonwealth of the United States, at any designated place of hearing.

(3) In case of contumacy by, or refusal to obey a subpoena issued to, any person, the Attorney General may invoke the aid of any court of the United States within the jurisdiction of which such investigation or proceeding is carried on, or where such person resides or carries on business, in requiring the attendance and testimony of witnesses and the production of books, papers, or other documents. Any such court may issue an order requiring such person to appear before the Attorney General or his designee, there to produce records, if so ordered, or to give testimony touching the matter under investigation. Any failure to obey such order of the court may be punished by such court as a contempt thereof.

(4) All process in any such case may be served in the judicial district in which such person resides or may be found. The Attorney General may make such rules relating to civil investigations as may be necessary or appropriate to implement the provisions of this subsection.

(e) Penalties

(1) (A) Any juridical person that violates subsection (a) of this section shall be fined not more than $2,000,000.

(B) Any juridical person that violates subsection (a) of this section shall be subject to a civil penalty of not more than $10,000 imposed in an action brought by the Attorney General.

(2) (A) Any natural person who willfully violates subsection (a) of this section shall be fined not more than $100,000 or imprisoned not more than 5 years, or both.

(B) Any natural person who violates subsection (a) of this section shall be subject to a civil penalty of not more than $10,000 imposed in an action brought by the Attorney General.

(3) Whenever a fine is imposed under paragraph (2) upon any officer, director, employee, agent, or stockholder of a person, such fine may not be paid, directly or indirectly, by such person.

(f) Definitions

For purposes of this section:

(1) The term “person,” when referring to an offender, means any natural person other than a. national of the United States (as defined in 8 U.S.C. § 1101) or any corporation, partnership, association, joint-stock company, business trust, unincorporated organization, or sole proprietorship organized under the law of a foreign nation or a political subdivision thereof

(2) (A) The term “foreign official” means any officer or employee of a foreign government or any department, agency, or instrumentality thereof, or of a public international organization, or any person acting in an official capacity for or on behalf of any such government or department, agency, or instrumentality, or for or on behalf of any such public international organization.

For purposes of subparagraph (A), the term "public international organization" means --

(i) an organization that has been designated by Executive Order pursuant to Section 1 of the International Organizations Immunities Act (22 U.S.C. § 288); or

(ii) any other international organization that is designated by the President by Executive order for the purposes of this section, effective as of the date of publication of such order in the Federal Register.

(3) (A) A person’s state of mind is "knowing"with respect to conduct, a circumstance, or a result if --

(i) such person is aware that such person is engaging in such conduct, that such circumstance exists, or that such result is substantially certain to occur; or

(ii) such person has a firm belief that such circumstance exists or that such result is substantially certain to occur.

(B) When knowledge of the existence of a particular circumstance is required for an offense, such knowledge is established if a person is aware of a high probability of the existence of such circumstance, unless the person actually believes that such circumstance does not exist.

(4) (A) The term "routine governmental action"means only an action which is ordinarily and commonly performed by a foreign official in--

(i) obtaining permits, licenses, or other official documents to qualify a person to do business in a foreign country;

(ii) processing governmental papers, such as visas and work orders;

(iii) providing police protection, mail pick-up and delivery, or scheduling inspections associated with contract performance or inspections related to transit of goods across country;

(iv) providing phone service, power and water supply, loading and unloading cargo, or protecting perishable products or commodities from deterioration; or

(v) actions of a similar nature.

(B) The term “routine governmental action” does not include any decision by a foreign official whether, or on what terms, to award new business to or to continue business with a particular party, or any action taken by a foreign official involved in the decision-making process to encourage a decision to award new business to or continue business with a particular party.

(5) The term “interstate commerce” means trade, commerce, transportation, or communication among the several States, or between any foreign country and any State or between any State

and any place or ship outside thereof, and such term includes the intrastate use of —

(A) a telephone or other interstate means of communication, or

(B) any other interstate instrumentality.

§ 78ff. Penalties

(a) Willful violations; false and misleading statements

Any person who willfully violates any provision of this chapter (other than section 78dd-1 of this title), or any rule or regulation thereunder the violation of which is made unlawful or the observance of which is required under the terms of this chapter, or any person who willfully and knowingly makes, or causes to be made, any statement in any application, report, or document required to be filed under this chapter or any rule or regulation thereunder or any undertaking contained in a registration statement as provided in subsection (d) of section 78*o* of this title, or by any self-regulatory organization in connection with an application for membership or participation therein or to become associated with a member thereof, which statement was false or misleading with respect to any material fact, shall upon conviction be fined not more than $5,000,000, or imprisoned not more than 20 years, or both, except that when such person is a person other than a natural person, a fine not exceeding $25,000,000 may be imposed; but no person shall be subject to imprisonment under this section for the violation of any rule or regulation if he proves that he had no knowledge of such rule or regulation.

(b) Failure to file information, documents, or reports

Any issuer which fails to file information, documents, or reports required to be filed under subsection (d) of section 78*o* of this title or any rule or regulation thereunder shall forfeit to the United States the sum of $100 for each and every day such failure to file shall continue. Such forfeiture, which shall be in lieu of any criminal penalty for such failure to file which might be deemed to arise under subsection (a) of this section, shall be payable into the Treasury of the United States and shall be recoverable in a civil suit in the name of the United States.

(c) Violations by issuers, officers, directors, stockholders, employees, or agents of issuers

(1) (A) Any issuer that violates subsection (a) or (g) of section 30A of this title [15 U.S.C. § 78dd-1] shall be fined not more than $2,000,000.

(B) Any issuer that violates subsection (a) or (g) of section 30A of this title [15 U.S.C. § 78dd-1] shall be subject to a civil penalty of not more than $10,000 imposed in an action brought by the Commission.

(2) (A) Any officer, director, employee, or agent of an issuer, or stockholder acting on behalf of such issuer, who willfully violates subsection (a) or (g) of section 30A of this title [15 U.S.C. § 78dd-1] shall be fined not more than $100,000, or imprisoned not more than 5 years, or both.

(B) Any officer, director, employee, or agent of an issuer, or stockholder acting on behalf of such issuer, who violates subsection (a) or (g) of section 30A of this title [15 U.S.C. § 78dd-1] shall be subject to a civil penalty of not more than $10,000 imposed in an action brought by the Commission.

(3) Whenever a fine is imposed under paragraph (2) upon any officer, director, employee, agent, or stockholder of an issuer, such fine may not be paid, directly or indirectly, by such issuer.

Statute

[As of July 22, 2004]

Anti-Bribery and Books & Records Provisions of

The Foreign Corrupt Practices Act

Current through Pub. L. 105-366 (November 10, 1998)

UNITED STATES CODE

TITLE 15. COMMERCE AND TRADE

CHAPTER 2B--SECURITIES EXCHANGES

§ 78m. Periodical and other reports

(a) Reports by issuer of security; contents

Every issuer of a security registered pursuant to section 78l of this title shall file with the Commission, in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate for the proper protection of investors and to insure fair dealing in the security--

(1) such information and documents (and such copies thereof) as the Commission shall require to keep reasonably current the information and documents required to be included in or filed with an application or registration statement filed pursuant to section 78l of this title, except that the Commission may not require the filing of any material contract wholly executed before July 1, 1962.

(2) such annual reports (and such copies thereof), certified if required by the rules and regulations of the Commission by independent public accountants, and such quarterly reports (and such copies thereof), as the Commission may prescribe.

Every issuer of a security registered on a national securities exchange shall also file a duplicate original of such information, documents, and reports with the exchange.

(b) Form of report; books, records, and internal accounting; directives

* * *

(2) Every issuer which has a class of securities registered pursuant to section 78l of this title and every issuer which is required to file reports pursuant to section 78o(d) of this title shall--

(A) make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer; and

(B) devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that--

(i) transactions are executed in accordance with management's general or specific authorization;

(ii) transactions are recorded as necessary (I) to permit preparation of financial statements in conformity with generally accepted accounting principles or any other criteria applicable to such statements, and (II) to maintain accountability for assets;

(iii) access to assets is permitted only in accordance with management's general or specific authorization; and

(iv) the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences.

(3) (A) With respect to matters concerning the national security of the United States, no duty or liability under paragraph (2) of this subsection shall be imposed upon any person acting in cooperation with the head of any Federal department or agency responsible for such matters if such act in cooperation with such head of a department or agency was done upon the specific, written directive of the head of such department or agency pursuant to Presidential authority to issue such directives. Each directive issued under this paragraph shall set forth the specific facts and circumstances with respect to which the provisions of this paragraph are to be invoked. Each such directive shall, unless renewed in writing, expire one year after the date of issuance.

(B) Each head of a Federal department or agency of the United States who issues such a directive pursuant to this paragraph shall maintain a complete file of all such directives and shall, on October 1 of each year, transmit a summary of matters covered by such directives in force at any time during the previous year to the Permanent Select Committee on Intelligence of the House of Representatives and the Select Committee on Intelligence of the Senate.

(4) No criminal liability shall be imposed for failing to comply with the requirements of paragraph (2) of this subsection except as provided in paragraph (5) of this subsection.

(5) No person shall knowingly circumvent or knowingly fail to implement a system of internal accounting controls or knowingly falsify any book, record, or account described in paragraph (2).

(6) Where an issuer which has a class of securities registered pursuant to section 78l of this title or an issuer which is required to file reports pursuant to section 78o(d) of this title holds 50 per centum or less of the voting power with respect to a domestic or foreign firm, the provisions of paragraph (2) require only that the issuer proceed in good faith to use its influence, to the extent reasonable under the issuer's circumstances, to cause such domestic or foreign firm to devise and maintain a system of internal accounting controls consistent with paragraph (2). Such circumstances include the relative degree of the issuer's ownership of the domestic or foreign firm and the laws and practices governing the business operations of the country in which such firm is located. An issuer which demonstrates good faith efforts to use such influence shall be conclusively presumed to have complied with the requirements of paragraph (2).

(7) For the purpose of paragraph (2) of this subsection, the terms "reasonable assurances" and "reasonable detail" mean such level of detail and degree of assurance as would satisfy prudent officials in the conduct of their own affairs.

* * *

§ 78dd-1 [Section 30A of the Securities & Exchange Act of 1934].

Prohibited foreign trade practices by issuers

(a) Prohibition

It shall be unlawful for any issuer which has a class of securities registered pursuant to section 78l of this title or which is required to file reports under section 78o(d) of this title, or for any officer, director, employee, or agent of such issuer or any stockholder thereof acting on behalf of such issuer, to make use of the mails or any means or instrumentality of interstate commerce corruptly in furtherance of an offer, payment, promise to pay, or authorization of the payment of any money, or offer, gift, promise to give, or authorization of the giving of anything of value to--

(1) any foreign official for purposes of--

(A) (i) influencing any act or decision of such foreign official in his official capacity, (ii) inducing such foreign official to do or omit to do any act in violation of the lawful duty of such official, or (iii) securing any improper advantage; or

(B) inducing such foreign official to use his influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality,

in order to assist such issuer in obtaining or retaining business for or with, or directing business to, any person;

(2) any foreign political party or official thereof or any candidate for foreign political office for purposes of--

(A) (i) influencing any act or decision of such party, official, or candidate in its or his official capacity, (ii) inducing such party, official, or candidate to do or omit to do an act in violation of the lawful duty of such party, official, or candidate, or (iii) securing any improper advantage; or

(B) inducing such party, official, or candidate to use its or his influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality.

in order to assist such issuer in obtaining or retaining business for or with, or directing business to, any person; or

(3) any person, while knowing that all or a portion of such money or thing of value will be offered, given, or promised, directly or indirectly, to any foreign official, to any foreign political party or official thereof, or to any candidate for foreign political office, for purposes of--

(A) (i) influencing any act or decision of such foreign official, political party, party official, or candidate in his or its official capacity, (ii) inducing such foreign official, political party, party official, or candidate to do or omit to do any act in violation of the lawful duty of such foreign official, political party, party official, or candidate, or (iii) securing any improper advantage; or

(B) inducing such foreign official, political party, party official, or candidate to use his or its influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality,

in order to assist such issuer in obtaining or retaining business for or with, or directing business to, any person.

(b) Exception for routine governmental action

Subsections (a) and (g) of this section shall not apply to any facilitating or expediting payment to a foreign official, political party, or party official the purpose of which is to expedite or to secure the performance of a routine governmental action by a foreign official, political party, or party official.

(c) Affirmative defenses

It shall be an affirmative defense to actions under subsection (a) or (g) of this section that--

(1) the payment, gift, offer, or promise of anything of value that was made, was lawful under the written laws and regulations of the foreign official's, political party's, party official's, or candidate's country; or

(2) the payment, gift, offer, or promise of anything of value that was made, was a reasonable and bona fide expenditure, such as travel and lodging expenses, incurred by or on behalf of a foreign official, party, party official, or candidate and was directly related to--

(A) the promotion, demonstration, or explanation of products or services; or

(B) the execution or performance of a contract with a foreign government or agency thereof.

(d) Guidelines by Attorney General

Not later than one year after August 23, 1988, the Attorney General, after consultation with the Commission, the Secretary of Commerce, the United States Trade Representative, the Secretary of State, and the Secretary of the Treasury, and after obtaining the views of all interested persons through public notice and comment procedures, shall determine to what extent compliance with this section would be enhanced and the business community would be assisted by further clarification of the preceding provisions of this section and may, based on such determination and to the extent necessary and appropriate, issue--

(1) guidelines describing specific types of conduct, associated with common types of export sales arrangements and business contracts, which for purposes of the Department of Justice's present enforcement policy, the Attorney General determines would be in conformance with the preceding provisions of this section; and

(2) general precautionary procedures which issuers may use on a voluntary basis to conform their conduct to the Department of Justice's present enforcement policy regarding the preceding provisions of this section.

The Attorney General shall issue the guidelines and procedures referred to in the preceding sentence in accordance with the provisions of subchapter II of chapter 5 of Title 5 and those guidelines and procedures shall be subject to the provisions of chapter 7 of that title.

(e) Opinions of Attorney General

(1) The Attorney General, after consultation with appropriate departments and agencies of the United States and after obtaining the views of all interested persons through public notice and comment procedures, shall establish a procedure to provide responses to specific inquiries by issuers concerning conformance of their conduct with the Department of Justice's present enforcement policy regarding the preceding provisions of this section. The Attorney General shall, within 30 days after receiving such a request, issue an opinion in response to that request. The opinion shall state whether or not certain specified prospective conduct would, for purposes of the Department of Justice's present enforcement policy, violate the preceding provisions of this section. Additional requests for opinions may be filed with the Attorney General regarding other specified prospective conduct that is beyond the scope of conduct specified in previous requests. In any action brought under the applicable provisions of this section, there shall be a rebuttable presumption that conduct, which is specified in a request by an issuer and for which the Attorney General has issued an opinion that such conduct is in conformity with the Department of Justice's present enforcement policy, is in compliance with the preceding provisions of this section. Such a presumption may be rebutted by a preponderance of the evidence. In considering the presumption for purposes of this paragraph, a court shall weight all relevant factors, including but not limited to whether the information submitted to the Attorney General was accurate and complete and whether it was within the scope of the conduct specified in any request received by the Attorney General. The Attorney General shall establish the procedure required by this paragraph in accordance with the provisions of subchapter II of chapter 5 of Title 5 and that procedure shall be subject to the provisions of chapter 7 of that title.

(2) Any document or other material which is provided to, received by, or prepared in the Department of Justice or any other department or agency of the United States in connection with a request by an issuer under the procedure established under paragraph (1), shall be exempt from disclosure under section 552 of Title 5 and shall not, except with the consent of the issuer, be made publicly available, regardless of whether the Attorney General responds to such a request or the issuer withdraws such request before receiving a response.

(3) Any issuer who has made a request to the Attorney General under paragraph (1) may withdraw such request prior to the time the Attorney General issues an opinion in response to such request. Any request so withdrawn shall have no force or effect.

(4) The Attorney General shall, to the maximum extent practicable, provide timely guidance concerning the Department of Justice's present enforcement policy with respect to the preceding provisions of this section to potential exporters and small businesses that are unable to obtain specialized counsel on issues pertaining to such provisions. Such guidance shall be limited to responses to requests under paragraph

(1) concerning conformity of specified prospective conduct with the Department of Justice's present enforcement policy regarding the preceding provisions of this section and general explanations of compliance responsibilities and of potential liabilities under the preceding provisions of this section.

(f) Definitions

For purposes of this section:

(1) A) The term "foreign official" means any officer or employee of a foreign government or any department, agency, or instrumentality thereof, or of a public international organization, or any person acting in an official capacity for or on behalf of any such government or department, agency, or instrumentality, or for or on behalf of any such public international organization.

(B) For purposes of subparagraph (A), the term "public international organization" means--

(i) an organization that is designated by Executive Order pursuant to section 1 of the International Organizations Immunities Act (22 U.S.C. § 288); or

(ii) any other international organization that is designated by the President by Executive order for the purposes of this section, effective as of the date of publication of such order in the Federal Register.

(2) (A) A person's state of mind is "knowing" with respect to conduct, a circumstance, or a result if--

(i) such person is aware that such person is engaging in such conduct, that such circumstance exists, or that such result is substantially certain to occur; or

(ii) such person has a firm belief that such circumstance exists or that such result is substantially certain to occur.

(B) When knowledge of the existence of a particular circumstance is required for an offense, such knowledge is established if a person is aware of a high probability of the existence of such circumstance, unless the person actually believes that such circumstance does not exist.

(3) (A) The term "routine governmental action" means only an action which is ordinarily and commonly performed by a foreign official in--

(i) obtaining permits, licenses, or other official documents to qualify a person to do business in a foreign country;

(ii) processing governmental papers, such as visas and work orders;

(iii) providing police protection, mail pick-up and delivery, or scheduling inspections associated with contract performance or inspections related to transit of goods across country;

(iv) providing phone service, power and water supply, loading and unloading cargo, or protecting perishable products or commodities from deterioration; or

(v) actions of a similar nature.

(B) The term "routine governmental action" does not include any decision by a foreign official whether, or on what terms, to award new business to or to continue business with a particular party, or any action taken by a foreign official involved in the decision-making process to encourage a decision to award new business to or continue business with a particular party.

(g) Alternative Jurisdiction

(1) It shall also be unlawful for any issuer organized under the laws of the United States, or a State, territory, possession, or commonwealth of the United States or a political subdivision thereof and which has a class of securities registered pursuant to section 12 of this title or which is required to file reports under section 15(d) of this title, or for any United States person that is an officer, director, employee, or agent of such issuer or a stockholder thereof acting on behalf of such issuer, to corruptly do any act outside the United States in furtherance of an offer, payment, promise to pay, or authorization of the payment of any money, or offer, gift, promise to give, or authorization of the giving of anything of value to any of the persons or entities set forth in paragraphs (1), (2), and (3) of this subsection (a) of this section for the purposes set forth therein, irrespective of whether such issuer or such officer, director, employee, agent, or stockholder makes use of the mails or any means or instrumentality of interstate commerce in furtherance of such offer, gift, payment, promise, or authorization.

(2) As used in this subsection, the term "United States person" means a national of the United States (as defined in section 101 of the Immigration and Nationality Act (8 U.S.C. § 1101)) or any corporation, partnership, association, joint-stock company, business trust, unincorporated organization, or sole proprietorship organized under the laws of the United States or any State, territory, possession, or commonwealth of the United States, or any political subdivision thereof.

§ 78dd-2. Prohibited foreign trade practices by domestic concerns

(a) Prohibition

It shall be unlawful for any domestic concern, other than an issuer which is subject to section 78dd-1 of this title, or for any officer, director, employee, or agent of such domestic concern or any stockholder thereof acting on behalf of such domestic concern, to make use of the mails or any means or instrumentality of interstate commerce corruptly in furtherance of an offer, payment, promise to pay, or authorization of the payment of any money, or offer, gift, promise to give, or authorization of the giving of anything of value to--

(1) any foreign official for purposes of--

(A) (i) influencing any act or decision of such foreign official in his official capacity, (ii) inducing such foreign official to do or omit to do any act in violation of the lawful duty of such official, or (iii) securing any improper advantage; or

(B) inducing such foreign official to use his influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality,

in order to assist such domestic concern in obtaining or retaining business for or with, or directing business to, any person;

(2) any foreign political party or official thereof or any candidate for foreign political office for purposes of--

(A) (i) influencing any act or decision of such party, official, or candidate in its or his official capacity, (ii) inducing such party, official, or candidate to do or omit to do an act in violation of the lawful duty of such party, official, or candidate, or (iii) securing any improper advantage; or

(B) inducing such party, official, or candidate to use its or his influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality,

in order to assist such domestic concern in obtaining or retaining business for or with, or directing business to, any person;

(3) any person, while knowing that all or a portion of such money or thing of value will be offered, given, or promised, directly or indirectly, to any foreign official, to any foreign political party or official thereof, or to any candidate for foreign political office, for purposes of--

(A) (i) influencing any act or decision of such foreign official, political party, party official, or candidate in his or its official capacity, (ii) inducing such foreign official, political party, party official, or candidate to do or omit to do any act in violation of the lawful duty of such foreign official, political party, party official, or candidate, or (iii) securing any improper advantage; or

(B) inducing such foreign official, political party, party official, or candidate to use his or its influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality,

in order to assist such domestic concern in obtaining or retaining business for or with, or directing business to, any person.

(b) Exception for routine governmental action

Subsections (a) and (i) of this section shall not apply to any facilitating or expediting payment to a foreign official, political party, or party official the purpose of which is to expedite or to secure the performance of a routine governmental action by a foreign official, political party, or party official.

(c) Affirmative defenses

It shall be an affirmative defense to actions under subsection (a) or (i) of this section that--

(1) the payment, gift, offer, or promise of anything of value that was made, was lawful under the written laws and regulations of the foreign official's, political party's, party official's, or candidate's country; or

(2) the payment, gift, offer, or promise of anything of value that was made, was a reasonable and bona fide expenditure, such as travel and lodging expenses, incurred by or on behalf of a foreign official, party, party official, or candidate and was directly related to--

(A) the promotion, demonstration, or explanation of products or services; or

(B) the execution or performance of a contract with a foreign government or agency thereof.

(d) Injunctive relief

(1) When it appears to the Attorney General that any domestic concern to which this section applies, or officer, director, employee, agent, or stockholder thereof, is engaged, or about to engage, in any act or practice constituting a violation of subsection (a) or (i) of this section, the Attorney General may, in his discretion, bring a civil action in an appropriate district court of the United States to enjoin such act or practice, and upon a proper showing, a permanent injunction or a temporary restraining order shall be granted without bond.

(2) For the purpose of any civil investigation which, in the opinion of the Attorney General, is necessary and proper to enforce this section, the Attorney General or his designee are empowered to administer oaths and affirmations, subpoena witnesses, take evidence, and require the production of any books, papers, or other documents which the Attorney General deems relevant or material to such investigation. The attendance of witnesses and the production of documentary evidence may be required from any place in the United States, or any territory, possession, or commonwealth of the United States, at any designated place of hearing.

(3) In case of contumacy by, or refusal to obey a subpoena issued to, any person, the Attorney General may invoke the aid of any court of the United States within the jurisdiction of which such investigation or proceeding is carried on, or where such person resides or carries on business, in requiring the attendance and testimony of witnesses and the production of books, papers, or other documents. Any such court may issue an order requiring such person to appear before the Attorney General or his designee, there to produce records, if so ordered, or to give testimony touching the matter under investigation. Any failure to obey such order of the court may be punished by such court as a contempt thereof.

All process in any such case may be served in the judicial district in which such person resides or may be found. The Attorney General may make such rules relating to civil investigations as may be necessary or appropriate to implement the provisions of this subsection.

(e) Guidelines by Attorney General

Not later than 6 months after August 23, 1988, the Attorney General, after consultation with the Securities and Exchange Commission, the Secretary of Commerce, the United States Trade Representative, the Secretary of State, and the Secretary of the Treasury, and after obtaining the views of all interested persons through public notice and comment procedures, shall determine to what extent compliance with this section would be enhanced and the business community would be assisted by further clarification of the preceding provisions of this section and may, based on such determination and to the extent necessary and appropriate, issue--

(1) guidelines describing specific types of conduct, associated with common types of export sales arrangements and business contracts, which for purposes of the Department of Justice's present enforcement policy, the Attorney General determines would be in conformance with the preceding provisions of this section; and

(2) general precautionary procedures which domestic concerns may use on a voluntary basis to conform

their conduct to the Department of Justice's present enforcement policy regarding the preceding provisions of this section.

The Attorney General shall issue the guidelines and procedures referred to in the preceding sentence in accordance with the provisions of subchapter II of chapter 5 of Title 5 and those guidelines and procedures shall be subject to the provisions of chapter 7 of that title.

(f) Opinions of Attorney General

(1) The Attorney General, after consultation with appropriate departments and agencies of the United States and after obtaining the views of all interested persons through public notice and comment procedures, shall establish a procedure to provide responses to specific inquiries by domestic concerns concerning conformance of their conduct with the Department of Justice's present enforcement policy regarding the preceding provisions of this section. The Attorney General shall, within 30 days after receiving such a request, issue an opinion in response to that request. The opinion shall state whether or not certain specified prospective conduct would, for purposes of the Department of Justice's present enforcement policy, violate the preceding provisions of this section. Additional requests for opinions may be filed with the Attorney General regarding other specified prospective conduct that is beyond the scope of conduct specified in previous requests. In any action brought under the applicable provisions of this section, there shall be a rebuttable presumption that conduct, which is specified in a request by a domestic concern and for which the Attorney General has issued an opinion that such conduct is in conformity with the Department of Justice's present enforcement policy, is in compliance with the preceding provisions of this section. Such a presumption may be rebutted by a preponderance of the evidence. In considering the presumption for purposes of this paragraph, a court shall weigh all relevant factors, including but not limited to whether the information submitted to the Attorney General was accurate and complete and whether it was within the scope of the conduct specified in any request received by the Attorney General. The Attorney General shall establish the procedure required by this paragraph in accordance with the provisions of subchapter II of chapter 5 of Title 5 and that procedure shall be subject to the provisions of chapter 7 of that title.

(2) Any document or other material which is provided to, received by, or prepared in the Department of Justice or any other department or agency of the United States in connection with a request by a domestic concern under the procedure established under paragraph (1), shall be exempt from disclosure under section 552 of Title 5 and shall not, except with the consent of the domestic concern, by made publicly available, regardless of whether the Attorney General response to such a request or the domestic concern withdraws such request before receiving a response.

(3) Any domestic concern who has made a request to the Attorney General under paragraph (1) may withdraw such request prior to the time the Attorney General issues an opinion in response to such request. Any request so withdrawn shall have no force or effect.

(4) The Attorney General shall, to the maximum extent practicable, provide timely guidance concerning the Department of Justice's present enforcement policy with respect to the preceding provisions of this section to potential exporters and small businesses that are unable to obtain specialized counsel on issues pertaining to such provisions. Such guidance shall be limited to responses to requests under paragraph (1) concerning conformity of specified prospective conduct with the Department of Justice's present enforcement policy regarding the preceding provisions of this section and general explanations of compliance responsibilities and of potential liabilities under the preceding provisions of this section.

(g) Penalties

(1)

(A) Any domestic concern that is not a natural person and that violates subsection (a) or (i) of this section shall be fined not more than $2,000,000.

(B) Any domestic concern that is not a natural person and that violates subsection (a) or (i) of this section shall be subject to a civil penalty of not more than $10,000 imposed in an action brought by the Attorney General.

(2)

(A) Any natural person that is an officer, director, employee, or agent of a domestic concern, or stockholder acting on behalf of such domestic concern, who willfully violates subsection (a) or (i) of this section shall be fined not more than $100,000 or imprisoned not more than 5 years, or both.

(B) Any natural person that is an officer, director, employee, or agent of a domestic concern, or stockholder acting on behalf of such domestic concern, who violates subsection (a) or (i) of this section shall be subject to a civil penalty of not more than $10,000 imposed in an action brought by the Attorney General.

(3) Whenever a fine is imposed under paragraph (2) upon any officer, director, employee, agent, or stockholder of a domestic concern, such fine may not be paid, directly or indirectly, by such domestic concern.

(h) Definitions

For purposes of this section:

(1) The term "domestic concern" means--

(A) any individual who is a citizen, national, or resident of the United States; and

(B) any corporation, partnership, association, joint-stock company, business trust, unincorporated organization, or sole proprietorship which has its principal place of business in the United States, or which is organized under the laws of a State of the United States or a territory, possession, or commonwealth of the United States.

(2)

(A) The term "foreign official" means any officer or employee of a foreign government or any department, agency, or instrumentality thereof, or of a public international organization, or any person acting in an official capacity for or on behalf of any such government or department, agency, or instrumentality, or for or on behalf of any such public international organization.

(B) For purposes of subparagraph (A), the term "public international organization" means --

(i) an organization that has been designated by Executive order pursuant to Section 1 of the International Organizations Immunities Act (22 U.S.C. § 288); or

(ii)any other international organization that is designated by the President by Executive order for the purposes of this section, effective as of the date of publication of such order in the Federal Register.

(3) (A) A person's state of mind is "knowing" with respect to conduct, a circumstance, or a result if--

(i) such person is aware that such person is engaging in such conduct, that such circumstance exists, or that such result is substantially certain to occur; or

(ii) such person has a firm belief that such circumstance exists or that such result is substantially certain to occur.

(B) When knowledge of the existence of a particular circumstance is required for an offense, such knowledge is established if a person is aware of a high probability of the existence of such circumstance, unless the person actually believes that such circumstance does not exist.

(4) (A) The term "routine governmental action"means only an action which is ordinarily and commonly performed by a foreign official in--

(i) obtaining permits, licenses, or other official documents to qualify a person to do business in a foreign country;

(ii) processing governmental papers, such as visas and work orders;

(iii) providing police protection, mail pick-up and delivery, or scheduling inspections associated with contract performance or inspections related to transit of goods across country;

(iv) providing phone service, power and water supply, loading and unloading cargo, or protecting perishable products or commodities from deterioration; or

(v) actions of a similar nature.

(B) The term "routine governmental action" does not include any decision by a foreign official whether, or on what terms, to award new business to or to continue business with a particular party, or any action taken by a foreign official involved in the decision-making process to encourage a decision to award new business to or continue business with a particular party.

(5) The term "interstate commerce"means trade, commerce, transportation, or communication among the several States, or between any foreign country and any State or between any State and any place or ship outside thereof, and such term includes the intrastate use of--

(A) a telephone or other interstate means of communication, or

(B) any other interstate instrumentality.

(i) Alternative Jurisdiction

(1) It shall also be unlawful for any United States person to corruptly do any act outside the United States in furtherance of an offer, payment, promise to pay, or authorization of the payment of any money, or offer, gift, promise to give, or authorization of the giving of anything of value to any of the persons or entities set forth in paragraphs (1), (2), and (3) of subsection (a), for the purposes set forth therein, irrespective of whether such United States person makes use of the mails or any means or instrumentality of interstate commerce in furtherance of such offer, gift, payment, promise, or authorization.

(2) As used in this subsection, a "United States person"means a national of the United States (as defined in section 101 of the Immigration and Nationality Act (8 U.S.C. § 1101)) or any corporation, partnership, association, joint-stock company, business trust, unincorporated organization, or sole proprietorship organized under the laws of the United States or any State, territory, possession, or commonwealth of the United States, or any political subdivision thereof.

§ 78dd-3. Prohibited foreign trade practices by persons other than issuers or domestic concerns

(a) Prohibition

It shall be unlawful for any person other than an issuer that is subject to section 30A of the Securities Exchange Act of 1934 or a domestic concern, as defined in section 104 of this Act), or for any officer, director, employee, or agent of such person or any stockholder thereof acting on behalf of such person, while in the territory of the United States, corruptly to make use of the mails or any means or instrumentality of interstate commerce or to do any other act in furtherance of an offer, payment, promise to pay, or authorization of the payment of any money, or offer, gift, promise to give, or authorization of the giving of anything of value to--

(1) any foreign official for purposes of--

(A) (i) influencing any act or decision of such foreign official in his official capacity, (ii) inducing such foreign official to do or omit to do any act in violation of the lawful duty of such official, or (iii) securing any improper advantage; or

(B) inducing such foreign official to use his influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality,

in order to assist such person in obtaining or retaining business for or with, or directing business to, any person;

(2) any foreign political party or official thereof or any candidate for foreign political office for purposes of--

(A) (i) influencing any act or decision of such party, official, or candidate in its or his official capacity, (ii) inducing such party, official, or candidate to do or omit to do an act in violation of the lawful duty of such party, official, or candidate, or (iii) securing any improper advantage; or

(B) inducing such party, official, or candidate to use its or his influence with a foreign government or

instrumentality thereof to affect or influence any act or decision of such government or instrumentality.

in order to assist such person in obtaining or retaining business for or with, or directing business to, any person; or

(3) any person, while knowing that all or a portion of such money or thing of value will be offered, given, or promised, directly or indirectly, to any foreign official, to any foreign political party or official thereof, or to any candidate for foreign political office, for purposes of--

(A) (i) influencing any act or decision of such foreign official, political party, party official, or candidate in his or its official capacity, (ii) inducing such foreign official, political party, party official, or candidate to do or omit to do any act in violation of the lawful duty of such foreign official, political party, party official, or candidate, or (iii) securing any improper advantage; or

(B) inducing such foreign official, political party, party official, or candidate to use his or its influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality,

in order to assist such person in obtaining or retaining business for or with, or directing business to, any person.

(b) Exception for routine governmental action

Subsection (a) of this section shall not apply to any facilitating or expediting payment to a foreign official, political party, or party official the purpose of which is to expedite or to secure the performance of a routine governmental action by a foreign official, political party, or party official.

(c) Affirmative defenses

It shall be an affirmative defense to actions under subsection (a) of this section that--

(1) the payment, gift, offer, or promise of anything of value that was made, was lawful under the written laws and regulations of the foreign official's, political party's, party official's, or candidate's country; or

(2) the payment, gift, offer, or promise of anything of value that was made, was a reasonable and bona fide expenditure, such as travel and lodging expenses, incurred by or on behalf of a foreign official, party, party official, or candidate and was directly related to--

(A) the promotion, demonstration, or explanation of products or services; or

(B) the execution or performance of a contract with a foreign government or agency thereof.

(d) Injunctive relief

(1) When it appears to the Attorney General that any person to which this section applies, or officer, director, employee, agent, or stockholder thereof, is engaged, or about to engage, in any act or practice constituting a violation of subsection (a) of this section, the Attorney General may, in his discretion, bring a civil action in an appropriate district court of the United States to enjoin such act or practice, and upon a proper showing, a permanent injunction or a temporary restraining order shall be granted without bond.

(2) For the purpose of any civil investigation which, in the opinion of the Attorney General, is necessary and proper to enforce this section, the Attorney General or his designee are empowered to administer oaths and affirmations, subpoena witnesses, take evidence, and require the production of any books, papers, or other documents which the Attorney General deems relevant or material to such investigation. The attendance of witnesses and the production of documentary evidence may be required from any place in the United States, or any territory, possession, or commonwealth of the United States, at any designated place of hearing.

(3) In case of contumacy by, or refusal to obey a subpoena issued to, any person, the Attorney General may invoke the aid of any court of the United States within the jurisdiction of which such investigation or proceeding is carried on, or where such person resides or carries on business, in requiring the attendance and testimony of witnesses and the production of books, papers, or other documents. Any such court may issue an order requiring such person to appear before the Attorney General or his designee, there to produce records, if so ordered, or to give testimony touching the matter under investigation. Any failure to obey such order of the court may be punished by such court as a contempt thereof.

(4) All process in any such case may be served in the judicial district in which such person resides or may be found. The Attorney General may make such rules relating to civil investigations as may be necessary or appropriate to implement the provisions of this subsection.

(e) Penalties

(1)

(A) Any juridical person that violates subsection (a) of this section shall be fined not more than $2,000,000.

(B) Any juridical person that violates subsection (a) of this section shall be subject to a civil penalty of not more than $10,000 imposed in an action brought by the Attorney General.

(2)

(A) Any natural person who willfully violates subsection (a) of this section shall be fined not more than $100,000 or imprisoned not more than 5 years, or both.

(B) Any natural person who violates subsection (a) of this section shall be subject to a civil penalty of not more than $10,000 imposed in an action brought by the Attorney General.

(3) Whenever a fine is imposed under paragraph (2) upon any officer, director, employee, agent, or stockholder of a person, such fine may not be paid, directly or indirectly, by such person.

(f) Definitions

For purposes of this section:

(1) The term “person,” when referring to an offender, means any natural person other than a. national of the United States (as defined in 8 U.S.C. § 1101) or any corporation, partnership, association, joint-stock company, business trust, unincorporated organization, or sole proprietorship organized under the law of a foreign nation or a political subdivision thereof

(2)

(A) The term “foreign official” means any officer or employee of a foreign government or any department, agency, or instrumentality thereof, or of a public international organization, or any person acting in an official capacity for or on behalf of any such government or department, agency, or instrumentality, or for or on behalf of any such public international organization.

For purposes of subparagraph (A), the term "public international organization" means --

(i) an organization that has been designated by Executive Order pursuant to Section 1 of the International Organizations Immunities Act (22 U.S.C. § 288); or

(ii) any other international organization that is designated by the President by Executive order for the purposes of this section, effective as of the date of publication of such order in the Federal Register.

(3) (A) A person’s state of mind is "knowing"with respect to conduct, a circumstance, or a result if --

(i) such person is aware that such person is engaging in such conduct, that such circumstance exists, or that such result is substantially certain to occur; or

(ii) such person has a firm belief that such circumstance exists or that such result is substantially certain to occur.

(B) When knowledge of the existence of a particular circumstance is required for an offense, such knowledge is established if a person is aware of a high probability of the existence of such circumstance, unless the person actually believes that such circumstance does not exist.

(4) (A) The term "routine governmental action"means only an action which is ordinarily and commonly performed by a foreign official in--

(i) obtaining permits, licenses, or other official documents to qualify a person to do business in a foreign country;

(ii) processing governmental papers, such as visas and work orders;

(iii) providing police protection, mail pick-up and delivery, or scheduling inspections associated with contract performance or inspections related to transit of goods across country;

(iv) providing phone service, power and water supply, loading and unloading cargo, or protecting perishable products or commodities from deterioration; or

(v) actions of a similar nature.

(B) The term “routine governmental action” does not include any decision by a foreign official whether, or on what terms, to award new business to or to continue business with a particular party, or any action taken by a foreign official involved in the decision-making process to encourage a decision to award new business to or continue business with a particular party.

(5) The term “interstate commerce” means trade, commerce, transportation, or communication among the several States, or between any foreign country and any State or between any State and any place or ship outside thereof, and such term includes the intrastate use of —

(A) a telephone or other interstate means of communication, or

(B) any other interstate instrumentality.

§ 78ff. Penalties

(a) Willful violations; false and misleading statements

Any person who willfully violates any provision of this chapter (other than section 78dd-1 of this title), or any rule or regulation thereunder the violation of which is made unlawful or the observance of which is required under the terms of this chapter, or any person who willfully and knowingly makes, or causes to be made, any statement in any application, report, or document required to be filed under this chapter or any rule or regulation thereunder or any undertaking contained in a registration statement as provided in subsection (d) of section 78*o* of this title, or by any self-regulatory organization in connection with an application for membership or participation therein or to become associated with a member thereof, which statement was false or misleading with respect to any material fact, shall upon conviction be fined not more than $5,000,000, or imprisoned not more than 20 years, or both, except that when such person is a person other than a natural person, a fine not exceeding $25,000,000 may be imposed; but no person shall be subject to imprisonment under this section for the violation of any rule or regulation if he proves that he had no knowledge of such rule or regulation.

(b) Failure to file information, documents, or reports

Any issuer which fails to file information, documents, or reports required to be filed under subsection (d) of section 78*o* of this title or any rule or regulation thereunder shall forfeit to the United States the sum of $100 for each and every day such failure to file shall continue. Such forfeiture, which shall be in lieu of any criminal penalty for such failure to file which might be deemed to arise under subsection (a) of this section, shall be payable into the Treasury of the United States and shall be recoverable in a civil suit in the name of the United States.

(c) Violations by issuers, officers, directors, stockholders, employees, or agents of issuers

(1)

(A) Any issuer that violates subsection (a) or (g) of section 30A of this title [15 U.S.C. § 78dd-1] shall be fined not more than $2,000,000.

(B) Any issuer that violates subsection (a) or (g) of section 30A of this title [15 U.S.C. § 78dd-1] shall be subject to a civil penalty of not more than $10,000 imposed in an action brought by the Commission.

(2)

(A) Any officer, director, employee, or agent of an issuer, or stockholder acting on behalf of such issuer, who willfully violates subsection (a) or (g) of section 30A of this title [15 U.S.C. § 78dd-1] shall be fined not more than $100,000, or imprisoned not more than 5 years, or both.

(B) Any officer, director, employee, or agent of an issuer, or stockholder acting on behalf of such issuer, who violates subsection (a) or (g) of section 30A of this title [15 U.S.C. § 78dd-1] shall be subject to a civil penalty of not more than $10,000 imposed in an action brought by the Commission.

(3) Whenever a fine is imposed under paragraph (2) upon any officer, director, employee, agent, or stockholder of an issuer, such fine may not be paid, directly or indirectly, by such issuer.

ACC CLO THINKTANK
SUMMARY/OUTLINE OF DISCUSSION TOPICS

FCPA Enforcement- Success Strategies

The following outline is intended to provide a short overview of some of the issues at the heart of this discussion topic. There may be other issues we've not identified or perspectives on the identified issues that are not adequately represented in the outline: you should feel free to raise these additional thoughts, as you like. ***The outline is merely intended as a starting point to help you identify discussion topics and tee up your conversation. There is no expectation that all issues will be covered during the discussion; instead, you'll be asked to select those most interesting to you so that the group can develop a consensus agenda at the beginning of the meeting.***

A. Organizational Issues/Functional Responsibilities

1. Setting the Tone at the Top: What does 'tone-at-the-top' mean within your organization when it comes to setting the tone on anti-corruption/anti-bribery? Is it CEO and C-Suite level tone—or is it 'tone-at-the-middle' (e.g., business leaders in geographic locations around the world), a combination or other? What practices do you implement to communicate the organization's messages/expectations/requirements? If faced with a prosecutor inquiring about whether the company has an effective program to prevent and detect (and remediate) FCPA violations, what factors would you describe? What are the "must haves" in setting your company's tone?

2. Role of CLO & Law Department: What role(s) do the CLO and law department play with regard to the company's FCPA/anti-bribery programs?

- *CLO's Role:* What are the CLO's responsibilities when it comes to developing and implementing FCPA-related measures? When investigations or other problems arise, are in-house lawyers used in the investigation process, and if so, in what capacity? What role do you play in assisting the Board in overseeing compliance in this area? Is there a specific Board committee on point for oversight in this area (e.g., governance/compliance committee, audit committee, etc.)? Do you provide regular reports regarding FCPA compliance initiatives to the Board? Do you provide internal compliance certifications regarding FCPA-related matters?
- *Lead FCPA/International Trade Lawyer; Law Department's Role:* Does your law department have a lead lawyer specializing in FCPA/anti-bribery/international trade matters? Is this person considered the 'go-to' person for advice, guidance and policy development in this area? Does this person report directly to you? Is that a change in organizational structure? Does this person provide internal compliance certifications regarding FCPA-related matters? What is the role of the law department in developing and implementing the organization's FCPA/anti-bribery compliance programs? Is the law department 'on-point'—or does it play more of a supporting role to other compliance, controls or ethics groups lead outside of authority of the legal function?
- *Role of in-house lawyers outside of the home office:* What is your experience with regard to the role of in-house lawyers outside of your organization's home office? Do all in-house lawyers—regardless of where they sit-- have organizational reporting relationships that ultimately leads on a solid-line basis to you as CLO? What are the pros and cons of this?

How does "where the lawyer sits" impact how the law department ensures compliance in this area? Have you implemented practices to help support and maintain a consistent role of in-house lawyers located in jurisdictions other than the organization's corporate headquarters? What are the pros and cons of de-centralized vs. centralized leadership on this issue?

3. Ethics & Compliance Function(s): If your organization has a centralized ethics & compliance function, what role does it play with regard to FCPA/anti-bribery (e.g., communicating guidelines, developing/implementing training, investigating alleged violations, etc.)? Does it have a specialized anti-bribery function within the department? Does the ethics & compliance function report organizationally to the law department/you as CLO? Is this function on point for FCPA/anti-bribery oversight—or is point role handled by a lawyer within the law department or another executive leader within the company?

4. Chief Compliance /Ethics Officer: Does the company have a chief compliance/ethics officer? What is the scope of that person's role? Are you as CLO also the chief compliance/ethics officer? Is this a de facto role or a formal designation? What are the pros and cons of having the CLO as the Chief Compliance/Ethics Officer? Are FCPA-related issues within the scope of this person's role? To whom does the Chief Compliance/Ethics Officer report? Does the compliance/ethics officer have direct access (and/or an organizational reporting relationship) to the Board? Are the ethics/compliance officers' functions coordinated with the legal department, and if so, how?

5. Role of the Board; Oversight: How does the Board view its oversight role in this area? Does your Board have a designated committee that looks at these issues and what are the key focus areas for this committee? Are there 'filters' or policies outlining the types of matters that need to be brought to the attention of the Board (and corresponding time frames)? Have you developed a "rule" as to the level significance of an FCPA concern must rise to before it's brought to the Board?

6. Other groups: Are there other corporate stakeholders/departments that play a role in establishing and implementing the organization's FCPA-related programs?

- *Internal functional groups:* may include internal audit, finance, risk management, government relations, human resources, public affairs, corporate social responsibility officers, others—what key roles do they play?
- *Subsidiaries, Affiliates & External agents:* are there point persons within these entities responsible for ensuring compliance with and implementation of the organization's policies and systems in this area? What is the law department's role in supporting these efforts? What are the key challenges? Is your organization implementing/have you heard about best or leading practices in this area?

B. FCPA Prevention Practices

1. Policy; Global Approach: How/does your company implement and enforce anti-corruption/anti-bribery programs on a global level? Given the current trend in the U.S. for greater FCPA enforcement, are companies/law departments modifying current practices proactively, and if so, how?

- *Harmonization among jurisdictions:* What practices does your law department implement to monitor varying jurisdictional requirements (including FCPA, Inter-American Convention Against Corruption, OECD conventions, Canada's The Corruption of Foreign Public Officials Act, United Nations Convention Against Corruption, plus the matrix of local customs, practices and laws)? Is your organization's approach to develop a single set of standards and to harmonize the varying jurisdictional requirements and expectations in some way? Who makes decisions on how to harmonize requirements? How are these expectations communicated within the organization worldwide?
- *Setting Minimum Program Requirements for Global Programs:* If your organization has a global approach, does the program go beyond the minimum requirements in a given jurisdiction and use the most stringent requirements as a floor?
- *Key Policy/Standards/Principals/Guideline Elements:* Is the organization's program in the form of a policy, standard, principals or guidelines? Are they expectations or requirements? What are the key elements? Are they general or specific (e.g., does the document generally state the organization's position on anti-bribery/corruption or is it more specific—articulating standards or prohibitions on things like facilitating payments, kickbacks, conflicts of interest, political contributions, philanthropic contributions, gifts/hospitality, extortion, etc..)? What are the pros and cons of these approaches?
- *Treatment of Subsidiaries and Affiliates:* Do the organization's standards and policies extend to subsidiaries and affiliates? What are the challenges in implementing these expectations? What types of practices have you implemented to help ensure that these policies and expected conduct standards are effectively communicated and enforced? Do you require compliance certifications of leaders within these entities? What are the pros and cons of such certifications? Do you have written agreements with these entities?
- *Treatment of Agents, Commercial Intermediaries, Suppliers:* Does your organization provide its policies to these entities? Does the organization have written agreements that govern the relationships with these entities? Do they specifically address anti-bribery and prohibitions on assignment, and if so, how?
- *Reconciling business practices with local law and customs:* How does your organization reconcile business practice expectations in local jurisdictions with global organizational standards for ethical conduct?
- *Competitive concerns with local industries:* Does your organization have concerns regarding local industries or companies that may not implement global policies and instead follow local customs and practices that may be less restrictive? How do you address those concerns?
- *Differences for U.S.-based and non-U.S.-based companies:* Are/should there be differences in concerns and processes and practices for companies depending upon whether they are based within or outside of the United States? What might some of the key differences be?

2. Communications: How is your policy on FCPA compliance communicated throughout the organization (and, as applicable, to subsidiaries, affiliates, agents, intermediaries, suppliers, etc.)? How often are these communications reinforced? Are policies available via the organization's intranet—to all or only to some? How do you control and make clear to others (e.g., accountants, outside lawyers, vendors, etc.) the company's expectations in this area?

3. Training: Does your organization have specific anti-bribery/FCPA training tools/modules?

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- *Types of training:* What constitutes "training" on this issue?: Is training on ethics primarily web-based, in-person, via video; different types depending upon location around the world? Is FCPA-related training part of a larger module of general compliance training, or is it a free-standing training: why? Did the organization develop the training internally? Is it offered in multiple languages?
- *Who receives training:* all employees, including the C-Suite and in-house lawyers? Is training offered to the Board? Is training provided to external service providers, vendors, affiliates/subsidiaries/joint venture partners? Others?
- *Mandatory; Certifications:* Is this training mandatory (for all or for some)? Does it include a certification component? What's the required frequency for completing training modules (e.g., is it annually, bi-annually, as part of new hire orientation, other)? Does the organization track who has completed training and are there consequences for failing to complete required training?

4. Records; Internal Controls: What types of record-keeping practices is your organization implementing to accurately track payments and transactions? Who is charged with responsibility for maintaining these records? What type of training is provided to individuals on properly maintaining books and records? Who has access to them? Are the records regularly audited/how often? By whom (Internal Audit? Finance? others?)? Do agreements with third party intermediaries/agents/suppliers provide the right for the organization to inspect and audit their books and records? What are the pros and cons of including this type of provision? What are the greatest challenges in this area? Are you implementing/aware of best or leading practices in this area? Have you implemented practices to enhance efficiencies in this area, and if so, what type(s)?

5. Competence of Employees Who Interact with Government Officials (e.g., sales force, in-house lobbyists, project managers, etc..): Does your organization review the competence of its international representatives prior to placing them in situations where corruption may be an issue? Does your organization review an employee's family and or business relationships with foreign officials prior to their placement in the field? Does your organization periodically review the general business reputation and integrity of its employees within the foreign territory that they operate? If so, how? If not, should such a review process be put in place? Does your organization provide special training to foreign employees? What does that training entail? What is missing from the training program? Does your organization provide support systems on which the representative can rely and access when corruption issues arise?

- *Compensation and Payment***:** Is a representative's compensation considered against the prevailing market rate in his or her foreign territory? Is the payment unusually high in the foreign territory? Is there a company policy that governs how payments are made to foreign employees who interact with government officials? Are payments made in cash, or directly to a third country bank account? What policies are in place to ensure that the monies are properly tracked? What channels are available for reporting financial concerns? Is there a direct line to the Audit Committee? Is there a direct line to the CLO? Is there an opportunity to submit a confidential or anonymous report? Are there different mechanisms in place for different parts of the company or is your program implemented globally?

- *Monitoring Activities***:** Does your company monitor the activities of its employees in foreign territories? Who is responsible for the monitoring? How is it done? Formally? Or informally? Is a formal report produced? If not, should one be? Is the information circulated within the company? To the CCO, the CLO, the Board, others? Are there systems in place to evaluate the monitored behaviour for possible corruption "red flags"? What systems? Does the company follow up on the information with the employee? With others? Is all information with respect to the employee maintained in one file? Is the CLO immediately advised of any allegation of non-compliance with the corruption legislation?
- *Red Flags:* Does your company have a list of "red flag" behaviours? What does it consider "red flag" behaviour? Does its list include an employee's:

i. refusal to provide certain key information, such as ownership structure;
ii. refusal to confirm that it will abide with the corruption legislation;
iii. request to have his or her identity kept secret;
iv. family or business ties to foreign public officials;
v. request to alter or backdate invoices;
vi. request for large bonuses or substantial deposits at the beginning of a contract; and
vii. request to be paid by means other than wire transfer or cheque.

Are there other "red flags"? Should there avoidance be incorporated into company policies and contracts to avoid any resultant issues?

- *Disciplinary/Administrative Procedures:* In the event of a violation of a company anti-corruption policy, or the legislation, how does the company react? Can a representative be suspended from work, with or without pay, pending an investigation or resolution of the matter? May the employee be terminated? Will the employees be indemnified by the company for costs incurred as a result of such violations? Why, or why not? May the company sue the representative for damages where appropriate? When will it be appropriate?

6. Screening/Due Diligence re: Third Parties: What screening practices do you implement prior to entering into relationships with third parties (such as intermediaries, agents, suppliers)? Who performs the screening—do you perform it internally or do you engage an external service provider? What are the key factors included within the review? What types of provisions do you include within third party agreements to help promote compliance (e.g., anti-corruption representations, audit rights, restrictions on assignment, audit rights, unilateral right to terminate, etc.)? Who is responsible for managing these relationships? Do you require that third parties sign anti-bribery certifications? Is this a one-time certification or a periodic one? If periodic, how often? How/do you promote and transfer your ethical culture/compliance programs to these entities? How do you survey and/or assess effectiveness of their programs? Is it necessary or a wasted effort? How do you monitor and review these relationships?

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7. Mergers & Acquisitions- Due Diligence: Does the scope of M&A due diligence include inquiries/inspections designed to assess compliance with anti-bribery/corruption programs? What are the key areas/red flags that must be considered in connection with these reviews? What is the role of the law department? Is due diligence generally conducted by in-house counsel or is outside counsel generally on point? Who are the key players to include on the due diligence team in order to identify any red flags that may require attention? What are the key challenges? Have you implemented best or leading practices in this area?

8. Audits: Does your organization audit compliance with anti-bribery/corruption programs, legal requirements and policies? Who is on point for performing these audits? What types of expertise specialists are on the audit team? What is the role of the law department? How often are audits performed? Do audits primarily focus on organizational operations or do they also extend to subsidiaries/affiliates/third parties? What types of reports are generated? Who receives them/how often? Are reports made verbally or in writing? Is there technology available to help out? How does your organization leverage expertise in the organization to assist in identification, analysis and reporting of compliance risks? What types of scenarios trigger further analysis or re-evaluation?

C. Mechanisms for Reporting Concerns

1. Reporting Concerns; Policy: Does the company have a policy and mechanisms for allowing employees, contractors and/or others to report concerns?

- *Scope:* Is the policy global in scope or does it vary by jurisdiction/country? Is there a separate policy for reporting information on financial or accounting irregularities? Are there separate policies for reporting certain types of allegations (e.g., pursuant to SOX or other compliance-focused regulations)?
- *Mandatory vs. Expectation vs. Encouraged:* Is reporting encouraged or required? Does the program cover questions on ethical conduct as well as potential violations and/or criminal conduct? Are there different reporting standards (e.g., mandatory vs. encouraged) depending upon whether the concern relates to an ethical conduct question or a violation? How are reported concerns about "stupid, but legal" issues handled (assuming they may involve ERM issues)?
- *Nature of Reports; Confidentiality:* Is there a preference for verbal versus written reporting? What does your policy say regarding confidentiality of compliance reporting?
- *Whistleblower Considerations:* What types of whistleblower or non-retaliation protections are included in your program?
- *Do the expectations for reporting concerns extend to external service providers* (e.g., vendors, outside counsel, business partners, joint ventures, etc.)?

2. Channels; Implementation: What channels/methods are available for reporting concerns (e.g., helpline, reporting tools, interview and complaint procedures, open door policy, ombuds system, etc.)?

- *Helplines:* are these administered internally or externally? If externally, who/what function within the organization is on point to receive information on concerns received by the outside entity? If internally, who/what function is on point? Does it depend on the nature of the issue?
- *Role of Law Department:* What role does the law department play in receiving, evaluating and investigating ethics-related questions or concerns?
- *Role of Other Functional Groups:* What are the other functional groups play key roles in receiving and evaluating/investigating ethics-related questions or concerns?
- *Reporting-up:* How does the organization determine which issues to report up to senior management/the Board? What is the role of the CLO in this process?

3. Communicating Expectations to Employees; Certification: How does the company communicate its interest in encouraging/requiring employee reporting on conduct that may violate organizational policies/legal requirements regarding anti-bribery/corruption? Are employees and/or subsidiary representatives or third parties asked to periodically certify compliance with the company's policies and/or certify whether they are aware of ethical problems or issues? When are issues communicated to the Board (or a Board committee), and who communicates such issues?

4. Monitoring Compliance with Reporting Expectations; Metrics: What controls and programs do you have in place to ensure reporting on ethical considerations at a global level? How effective are they? How do you document implementation? Are your compliance and ethics measurement systems adequately designed to uncover red flags, warning the CLO of areas of concern in areas such as accounting and regulatory compliance? What checks and balances exist between the Board's committees, CLO and outside experts, such as accountants and consultants?

D. Internal Investigations/Response to Government Investigations/Reporting

1. Process for Determining Action: How are inquiries/reports of concerns regarding anti-bribery/corruption considerations filtered and investigated? Who makes decisions on strategy for addressing these concerns and internal investigations? What is the decision process for initiating an internal investigation? Who generally manages investigations within the company? Does the company have documented procedures for investigating alleged ethical concerns and/or violations? Is there a designated team or function on point to generally conduct preliminary internal investigations?

2. Role of CLO; Law Department: What is the role of the CLO/law department in connection with internal investigations of alleged ethical conduct violations? Does the law department generally lead these investigations or otherwise play a coordinating or supporting role? Would the law department's role change if the investigation is undertaken in response to a government inquiry versus as follow-up to an internal reported concern regarding a potential allegation of wrongdoing? Is privilege a consideration? What criteria are considered in determining whether to bring in outside investigators/outside counsel to help conduct or lead an investigation? How do you deal with legally mandated disclosures or voluntary disclosures? What role does the CLO play in communicating investigation outcomes to the Board and/or managing risk?

3. Board's Role: In light of the Board's fiduciary duty of care and loyalty, are quality controls in place for your Board institute to ensure that it understands and effectively performs its oversight role and monitoring of investigations?

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4. Additional Considerations- Documents; Attorneys Fees: Are investigations of anti-bribery/corruption allegations conducted with an understanding that the results and/or a written report will likely be provided to the government? Are they handled as other investigations are, or are there separate processes? Are reports provided or underlying facts discussed? How does this impact the scope and approach for conducting the investigation?

- What factors are considered in determining whether to prepare a written report?
- Is privilege an issue? What is the role of lawyers (in-house) on the investigative team?
- Are there two internal investigations (one that might be provided to the government and a second for which privilege may be claimed)?
- Guidance or training on performing the investigation and writing the report?
- How are corporate Miranda-type warnings provided to employee interviewees (verbally, in writing, signed statement, etc.)?
- What is the organization's policy on protecting / defending targeted employees? Has it changed in light of recent decisions in this area (US v. Stein)?

5. Multiple Cross-Border Investigations; Coordination: What are some of the key steps/additional factors to consider when multiple agencies are involved? How does your role as CLO/law department's role change? How do you manage multiple, multi-jurisdictional or cross-border investigations and the corresponding expectations of different regulators and law enforcement agencies? Under what circumstances would you choose to meet personally and/or be the point legal person for discussions with government regulators on enforcement investigations and cases? Do you engage multiple outside counsel depending upon the countries/agencies involved? What types of practices do you implement to coordinate your internal investigation and response team?

6. Public disclosure: When does the existence of an investigation trigger a disclosure obligation or a strategic decision to disclose to a regulatory agency/law enforcement? What standards have your law department and organization implemented to evaluate when disclosure is appropriate? What are the key challenges in making these determinations? What role do you play as CLO? Is your company's Board involved? Who can/should be told within a company (or at the Board level) about an investigation of anti-bribery/corruption misconduct allegations?

E. Enforcement Strategies; Remedial Actions; Self-Reporting

1. Remedial Actions within the Organization: What types of processes and practices has the company implemented to admonish misconduct in this area? Does the organization have disciplinary procedures to address violations of its ethics and compliance programs? Are they consistently applied? Do remedial actions vary and depend on the level of the culpable individual? Do/how do you communicate within the organization remedial steps taken to address confirmed allegations of misconduct? Who is on point (an executive team, the CLO, head of HR, Chief Ethics Officer, business leader of the affected business unit, other) to determine the appropriate course of action? What do you view as best practices in this area?

2. Remedial Actions Regarding Third Parties: What types of protections do you build into written agreements/arrangements with third parties to protect against misconduct in this area? What practices have been most effective? Do you reserve the right to inspect/audit? Does the audit team differ when auditing third parties versus organizational operations? What are some of the key steps taken to terminate/unwind the relationship? What are some of the key reporting considerations (internal and external to regulatory agencies)? What are the greatest challenges?

3. Self-Reporting to Regulators: What are the key criteria/drivers considered in making a decision to self-report to a regulatory agency? Who is involved in the ultimate decision-process? What is your role as CLO? What is the role of the Board? Who takes the lead in initiating reporting? Do you request the opportunity to report in person, via phone, other? What are some of the key considerations in determining whether an investigation of an allegation is 'ripe' to self-report? What are some of the pitfalls/best practices in self-reporting strategies?

4. Disclosing to Auditors: What are the key considerations in determining whether an allegation of potential misconduct/government inquiry into potential misconduct is appropriate/timely for disclosure to auditors? What types of practices have you implemented in making and implementing these disclosure decisions? Are these conversations or in writing? Is privilege protection a consideration? What are some of the key challenges?

5. Enforcement; Deferred Prosecution/Non-Prosecution Agreements: What are some of the strategies you've implemented or heard of in connection with successfully resolving enforcement actions relating to bribery/corruption? What are the most important provisions to include in any settlement/DPA/NPA? What are some of the most problematic provisions? What are the key steps to take in the early phases of the self-reporting/strategic resolution discussions? What are the regulators most concerned about? What types of remedial initiatives have they been most responsive to? When do you think monitors are appropriate? How do you think they should be selected? What do you view as the appropriate oversight of a DPA/NPA? What factors do you think the government considers most in determining whether to enter into a DPA or NPA? Additional ideas on challenges/success factors/leading practices in this area?

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REFERENCES

Following is a sampling of a variety of resources relating to our session topic. For additional ACC resources, search ACC's Virtual Library at www.acc.com/vl.

FCPA- GENERAL

Article: "Overseas Ventures and Adventures" (ACC Docket October 2007)
http://www.acc.com/resource/v8704

Article: "The Challenges of Global Compliance in Emerging Markets" (ACC Docket September 2007)
http://www.acc.com/resource/v8632

Article: "Small Bribes Buy Big Problems" (ACC Docket September 2007)
http://www.acc.com/resource/v8633

Article: "Compliance Programs for Importing and Exporting" (ACC Docket September 2007)
http://www.acc.com/resource/v8631

Article: "Bribes, Borders, and Bottom Lines: Why a Strong Anti-bribery Policy Is Essential" (ACC Docket September 2006)
http://www.acc.com/resource/v7523

Article: "Business Ethics—Awaken the Zombies!" (ACC Docket July/August 2006)
http://www.acc.com/resource/v7316

Article: "An Overview of the Foreign Corrupt Practices Act"
http://www.acc.com/resource/getfile.php?id=7904

Publication: "U.S. and PRC Anti-Bribery Laws: Regulation, Risk and Prevention in the Life Sciences Industries (Chapter from PLC Cross-border Life Sciences Handbook 2007/08)
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Program Material: "Anatomy of a Bribe" (ACC Annual Meeting 2007)
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Quick Reference: "FCPA Provisions and Sample Forms; Checklists Packet"
http://www.acc.com/resource/v7905

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White Paper: "Corporate Governance Programs for Reporting Concerns: What Companies are Doing"
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Article: "Managing an Internal Corporate Fraud Investigation & Prosecution" (ACC Docket April 2007)
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Article: "What to do When the Whistle Blows: the Ins & Outs of Internal Investigations" (ACC Docket May 2004)
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Article: "Interview with Comey re: DOJ Policy on Corporations Under Investigation"
http://www.justice.gov/usao/eousa/foia_reading_room/usab5106.pdf#search=%22u.s.%20attorney

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FCPA ENFORCEMENT

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Article: "Fifth Circuit Extends the Reach of the FCPA" (Sidley Update, November 13, 2007)
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Article: Recent SEC FCPA Cases Provide Guidance for Responding to the Discovery of Illicit Payments and Avoiding Improper Selective Disclosures (Sidley Update, October 4, 2007)
http://www.sidley.com/clientupdates/Detail.aspx?news=3328

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No. 08-01

Date: January 15, 2008

Foreign Corrupt Practices Act Review

Opinion Procedure Release

The Department has reviewed the FCPA Opinion Procedure request and supporting materials, dated January 2, 2008 (the "Request"), submitted by a United States issuer (the "Requestor") under the Foreign Corrupt Practices Act ("FCPA") Opinion Procedure, 28 C.F.R. Part 80. The facts and circumstances are as follows:

Overview of the Request

The Requestor is a Delaware corporation with its principal place of business in the United States, and an issuer within the meaning of the FCPA, 15 U.S.C. §§ 78dd-1, *et seq*. The Requestor has requested that the Department of Justice issue an Opinion under the FCPA Opinion Procedure, 28 C.F.R. Part 80, stating its enforcement policy with respect to the prospective majority investment by a wholly-owned foreign subsidiary of the Requestor in a foreign company that is responsible for managing certain public services for a major foreign municipality. This anticipated investment (the "Proposed Transaction") is described more fully below.

The Requestor notes that the Proposed Transaction is a matter of significant importance and urgency to the Requestor, this opportunity is highly valued, and delay by the Requestor in committing to the Proposed Transaction will likely forever preclude its consummation. Accordingly, the Requestor has asked that the Department of Justice consider this opinion request on an expedited basis. The Department of Justice has agreed to and conducted expedited review.

The Requestor: Background

The Requestor is a Fortune 500 company headquartered in the United States, located in over 35 countries, including the country at issue in this Request, and with worldwide annual revenues of several billion dollars. The Requestor's relevant business unit is one of the largest providers of the relevant public services to governments worldwide.

The Investment Target and Other Relevant Parties

The Requestor has made the following representations regarding the operation and ownership of the investment target company in the foreign country (the "Investment Target") and certain relevant parties:

Currently, the relevant public services for the foreign municipality are provided by the Investment Target. The Investment Target currently is jointly owned by a government-owned

entity of the foreign country (the "Foreign Government Owner") and a foreign private company (the "Foreign Private Company 1"). A citizen of the foreign country (the "Investment Target Chairman") is the Chairman and formal legal representative of the Investment Target.

The Foreign Government Owner, historically, is the majority owner of the Investment Target and currently holds a 56% ownership share in that company. The Foreign Government Owner's indirect majority parent is the foreign country's governmental entity generally responsible for the management, reform and restructuring of state-owned enterprises (the "State Enterprises Management Entity"). In particular, the State Enterprises Management Entity is responsible for determining from which state-owned companies the government should divest, and for effectuating public offerings or sales of state-owned assets through another governmental entity (the "State Enterprises Divestiture Entity").[1] In addition to his role at the Investment Target, the Investment Target Chairman is also the General Manager and formal legal representative of the Foreign Government Owner.

Foreign Private Company 1, established under the laws of the foreign country, is the 44% minority owner of the Investment Target. The controlling and ultimate beneficial owner, and the formal legal representative, of Foreign Private Company 1 is a citizen of the foreign country (the "Foreign Private Company Owner"). The Foreign Private Company Owner has substantial business experience in the foreign municipality, and in particular, with the relevant public services provided by the Investment Target. Foreign Private Company 1 has appointed the Foreign Private Company Owner as its representative in the Investment Target. In this role, the Foreign Private Company Owner holds the title of General Manager of the Investment Target. However, the Foreign Private Company Owner is not an employee of the Investment Target and receives no salary or other direct compensation from the Investment Target. Further, the Foreign Private Company Owner has no other formal affiliation with the host country government other than through his involvement in the Investment Target as its General Manager.

The Investment Target Divestiture and The Requestor's Business Opportunity

In its Request, the Requestor has described the origin of the investment opportunity as follows:

Some time prior to November 2007, the Foreign Government Owner and the State Enterprises Management Entity determined to divest the host country government's interest in the Investment Target and, thus, fully privatize the business. Around November 2007, the Foreign Government Owner received formal approval of the State Enterprises Management Entity for such divestiture and, as required under foreign law, the public bid process managed by the State Enterprises Divestiture Entity was initiated for the purpose of selling the entirety of the Foreign Government Owner's 56% share in the Investment Target. Pursuant to the host country government's regulations, the bids themselves were subject to review by the State Enterprises

[1] The State Enterprises Divestiture Entity is also owned and controlled by the State Enterprises Management Entity.

Divestiture Entity, the Foreign Government Owner, and the Foreign Government Owner's direct parent corporations. The Foreign Government Owner and its direct corporate parents have final authority to select and approve a final bid.[2]

After the announcement of the planned divestiture of the Investment Target shares, the Requestor engaged in substantial discussions with the Foreign Private Company Owner regarding the potential entrée of the Requestor into the market for the relevant public services in the foreign country. The Requestor determined that a potential controlling investment in the Investment Target presented an opportunity for a long-term, high-yield return of revenue and profit, and, perhaps more importantly, could provide an unparalleled competitive advantage by securing a foothold for the Requestor in the regional markets generally.

Prior Negotiations

The Requestor has made the following representations regarding the Requestor's prior negotiations with the Foreign Private Company Owner regarding the Investment Target, and the Requestor's identification of, and responses to, FCPA concerns identified in connection with the Proposed Transaction:

In late 2005, the Requestor was first contacted by the Investment Target's representatives who were searching for a foreign investor with relevant expertise. In approximately June 2006, the Requestor began direct discussions with the Foreign Private Company Owner in connection with a possible joint venture through which the Requestor would purchase a controlling interest in the Investment Target following the government's anticipated sale of its portion of the entity. The parties considered a scenario whereby: (1) the Foreign Private Company Owner (through a new company controlled and beneficially owned by him, the "Foreign Private Company 2") would obtain 100% ownership of the Investment Target by bidding on and hopefully obtaining the Foreign Government Owner's shares of the Investment Target through the State-sponsored sale, and by transferring Foreign Private Company 1's 44% interest to Foreign Private Company 2; and (2) the Requestor would then purchase a controlling interest in the Investment Target from Foreign Private Company 2.[3] Thus, this transaction would result in the Requestor acquiring a controlling interest in the Investment Target, while Foreign Private Company 2 and the Foreign Private Company Owner would retain a minority ownership interest.

[2] As described in more detail below, the bidding process is complete, but the divestiture has not yet been finalized.

[3] From a long-term financial perspective, the Requestor valued the potential controlling interest in the Investment Target at a significant premium above what the Requestor believed the Foreign Government Owner's shares would be sold for. Thus, the Requestor was prepared to purchase those shares at a substantial premium above their initial public purchase price.

The Requestor's Initial FCPA Concerns and Due Diligence Efforts

The Requestor has represented the following with respect to the due diligence efforts undertaken by it in connection with its potential purchase of a controlling interest in the Investment Target from Foreign Private Company 2, and the Requestor's assessment of the attendant FCPA risks:

Prior to executing a joint venture agreement with the Foreign Private Company Owner, the Requestor conducted due diligence of the potential joint venture to assess, among other things, potential FCPA-related risk. In conducting its due diligence, the Requestor understood that, as General Manager of the Investment Target, a joint venture whose majority owner is a state-owned company, the Foreign Private Company Owner would be considered a "foreign official" for purposes of the FCPA, 15 U.S.C. § 78dd-1(f)(1)(A). Accordingly, the Requestor sought to assure itself that any payment to the Foreign Private Company Owner for the Foreign Private Company 2 shares of the Investment Target would not be in violation of the FCPA, and that the Foreign Private Company Owner did not obtain those shares improperly under foreign law.

The due diligence conducted, none of which identified any negative information regarding the Foreign Private Company Owner, Foreign Private Company 1, or the Investment Target, including the following:

1. The Requestor commissioned a report on the Foreign Private Company Owner by a reputable international investigative firm.

2. The Requestor retained a business consultant in the foreign municipality who provided advice on possible due diligence procedures in the foreign country.

3. The Requestor commissioned International Company Profiles on the Investment Target and Foreign Private Company 1 from the U.S. Commercial Service of the Commerce Department.

4. The Requestor searched the names of all relevant persons and entities, including the Foreign Private Company Owner, the Investment Target, and Foreign Private Company 1, through the various services and databases accessible to the Requestor's International Trade Department -- including a private due diligence service -- to determine that no relevant parties are included on lists of designated or denied persons, terrorist watches, or similar designations.

5. The Requestor met with representatives of the U.S. Embassy in the foreign municipality and learned that there were no negative records at the Embassy regarding any party to the Proposed Transaction.

6. Outside counsel conducted due diligence and issued a preliminary report. An updated report is being prepared, and will be completed before closing the Proposed Transaction.

7. An outside forensic accounting firm has prepared a preliminary due diligence report and a final report is being prepared, and will be completed before closing the Proposed Transaction.

8. A second law firm has reviewed the due diligence.

The Requestor identified two principal FCPA-related risks to be addressed prior to its consummation of the Proposed Transaction. First, the Requestor originally believed that, as General Manager of the Investment Target, the Foreign Private Company Owner was subject to foreign certain foreign privatization regulations (the "privatization regulations"), and as such he could only legally participate in the purchase of the Foreign Government Owner's sale of its shares in the Investment Target if his ownership interests in Foreign Private Company 1 and Foreign Private Company 2 were adequately disclosed to the Foreign Government Owner and its State-owned parent organizations. Second, the Requestor believed that, as General Manager of the Investment Target, the Foreign Private Company Owner was legally prohibited from acting on corporate opportunities – for example, realizing the purchase price premium from the Requestor for the Investment Target shares – that arguably belonged to a government-owned entity (*i.e.,* the Foreign Government Owner), without first seeking approval from the Foreign Government Owner.

When presented with these issues by the Requestor in September 2007, the Foreign Private Company Owner, through counsel, declined to make or accede to disclosures to the Foreign Government Owner and its corporate parents regarding his various roles and beneficial interests for the stated reasons that in the foreign country it was neither necessary nor customary to do so. In addition, the Foreign Private Company Owner declined to disclose to the Foreign Government Owner and its corporate parents information concerning the premium the Requestor would agree to pay for the proposed controlling stake in the Investment Target. At the time, the Foreign Private Company Owner informed the Requestor that its disclosure requests were inconsistent with business practices in the foreign country and that competitive concerns prevented him from agreeing to disclose to the Foreign Government Owner and its corporate parents his bid price on the Investment Target or the spread between his bid and the price for which the Requestor would agree to purchase the controlling interest in the Investment Target.

Also at that time, the Requestor believed that the Foreign Private Company Owner's bid for the government-owned shares in the Investment Target had been accepted and that the State Enterprises Divestiture Entity-run sale of those shares would be finalized in the immediate future. In light of the Foreign Private Company Owner's reluctance to make what the Requestor believed were necessary disclosures, and because it did not appear to the Requestor that post-sale disclosures would be sufficient to bring the Foreign Private Company Owner's acquisition within the strictures of the foreign country's laws, the Requestor decided to abandon the proposed joint venture and so informed the Foreign Private Company Owner.

Resumption of Negotiations and Renewed FCPA Due Diligence

The Requestor has stated the following with respect to the facts and circumstances of the Requestor's resumption of negotiations with the Foreign Private Company Owner and additional due diligence efforts undertaken by the Requestor:

After a period of approximately three weeks, on or about November 1, 2007, the Foreign Private Company Owner requested that the Requestor renew negotiations of the Proposed Transaction. Without engaging the Foreign Private Company Owner in substantive negotiations, the Requestor first reiterated its concern over disclosure and the Foreign Private Company Owner's compliance with the privatization regulations. The Foreign Private Company Owner still resisted such disclosure, but also indicated his belief that, based on a conversation he had with an attorney at the State Enterprises Divestiture Entity (the "Divestiture Entity Lawyer"), the privatization regulations did not apply to him because he was not a paid manager of the Investment Target, but rather a voluntary minority-owner representative at the Investment Target with no real control over that entity. In response, prior to agreeing to renew negotiations of the Proposed Transaction, the Requestor sought to conduct additional due diligence to determine whether, or to what extent, its initial analysis of the application of the privatization regulations had been incorrect as to the Foreign Private Company Owner, and to verify his claims as to both the facts of his involvement at the Investment Target and the foreign law ramifications of the same. The Foreign Private Company Owner did not object to the Requestor's pursuit of these additional due diligence steps.

As part of that additional due diligence, the Requestor learned from the State Enterprises Divestiture Entity officials that although the Foreign Private Company Owner's bid for the Investment Target shares had been accepted by the Foreign Government Owner, the State Enterprises Divestiture Entity, and the State Enterprises Management Entity,[4] the Foreign Private Company Owner was providing the purchase money in installments and that, therefore, his purchase of the Investment Target had not yet been consummated. The Requestor viewed this fact as an opportunity to take affirmative steps as part of its additional due diligence to disclose, prior to finalization of the sale, The Foreign Private Company Owner's beneficial ownership interest in Foreign Private Company 1 and Foreign Private Company 2 to legal representatives and high-ranking officials of relevant government-owned entities. The Foreign Private Company Owner did not object to the Requestor's disclosures to government-owned entities regarding his role and the Proposed Transaction.

Thereafter, the Requestor met with various high-ranking relevant government officials, confirmed certain information, and made certain disclosures (both orally and in writing). First, the Requestor's representatives met with a senior official in the State Enterprises Divestiture Entity (the "Divestiture Entity Senior Official"), who explained that the State Enterprises

[4] The State Enterprises Divestiture Entity officials informed the Requestor that the Foreign Private Company Owner had submitted the only bid.

Divestiture Entity is responsible for managing the sales of government-owned assets, and that it reports to the State Enterprises Management Entity. As part of a State-owned asset sale, the State Enterprises Divestiture Entity is responsible for reviewing the forms required to be filed by the seller, including reviewing paperwork for purposes of determining compliance with the privatization regulations. The Requestor's representatives disclosed to the Divestiture Entity Senior Official that: (1) the Requestor had been negotiating with the Foreign Private Company Owner for over a year to purchase a majority interest in the Investment Target; (2) the Foreign Private Company Owner was in the process of buying the Foreign Government Owner shares in the Investment Target through a the State Enterprises Divestiture Entity-run State asset sale; (3) the Foreign Private Company Owner is the current minority beneficial shareholder of the Investment Target and is the General Manager of the Investment Target; and (4) the Requestor is offering the Foreign Private Company Owner a very substantial price premium over the price the Foreign Private Company Owner has agreed to pay for the Foreign Government Owner's shares of the Investment Target. During the meeting, the Divestiture Entity Senior Official expressed no reservations about the appropriateness of the Proposed Transaction and commented specifically that the premium described would not be unusual or unexpected. Subsequent to this meeting, the Requestor reiterated these disclosures by letter to the Divestiture Entity Senior Official.

Soon thereafter, the Requestor's representatives met with a lawyer for the State Enterprises Divestiture Entity (the "Divestiture Entity Lawyer") and disclosed the same details of the Proposed Transaction as had been relayed to the Divestiture Entity Senior Official. The Divestiture Entity Lawyer explained that the Foreign Private Company Owner had been selected as the winning bidder in the Investment Target tender, but that the Foreign Private Company Owner was making payments for the tendered shares in installments and that, as such, the sale and transfer of shares was not complete. Further, the Divestiture Entity Lawyer explained that the State Enterprises Divestiture Entity reviewed the Foreign Private Company Owner's bid in light of potential restrictions under the privatization regulations when the bid process formally began in September 2007, and that the State Enterprises Divestiture Entity had determined that the Foreign Private Company Owner was not a government official for purposes of those regulations because the Foreign Private Company Owner served as General Manager of the Investment Target only in his capacity as the representative of the minority, private owners of the Investment Target shares. The Divestiture Entity Lawyer represented that he personally had confirmed this interpretation of the privatization regulations with a senior official with the State Enterprises Divestiture Entity department responsible for ensuring that the public tender process is run consistent with the State Enterprises Divestiture Entity's procedures. Subsequent to this meeting, via letter to the Divestiture Entity Lawyer, the Requestor reiterated the disclosures noted above.

That same date, representatives of the Requestor met with the Investment Target Chairman. The Foreign Private Company Owner also attended this meeting. The Requestor disclosed to the Investment Target Chairman the same details of the Proposed Transaction as had been relayed to the Divestiture Entity Senior Official and the Divestiture Entity Lawyer. Specifically, the Requestor inquired whether the Investment Target Chairman was aware of the Foreign Private

Company Owner's various roles in the Investment Target and Foreign Private Companies 1 and 2, whether the Investment Target Chairman believed the privatization regulations applied to and precluded the Foreign Private Company Owner's participation, and whether the Investment Target Chairman was aware of the substantial premium the Requestor was prepared to offer the Foreign Private Company Owner. The Investment Target Chairman indicated that: (1) he was previously aware of the Foreign Private Company Owner's role as General Manager and minority shareholder of the existing joint venture; (2) he was previously aware of the Foreign Private Company Owner's role as the shareholder of the acquiring entity (Foreign Private Company 2); (3) he did not believe that the privatization regulations applied to the Foreign Private Company Owner in this context because he, the Investment Target Chairman, was the Senior Manager at the Investment Target, and not the Foreign Private Company Owner; and (4) he understood that the Requestor would pay a substantial premium for the Investment Target shares, and he had no objections.[5] Subsequent to this meeting, by letter to the Investment Target Chairman, the Requestor reiterated the oral disclosures and confirmed the substance of the parties' discussions.

Finally, representatives of the Requestor met with staff members of the State Enterprises Divestiture Entity and a supervisor in the State-Owned Asset Department of the State Enterprises Divestiture Entity. The Requestor's representatives disclosed to these officials the same details of the Proposed Transaction as had been relayed in each of the prior meetings described above. One staff member explained that her department at the State Enterprises Divestiture Entity was responsible for determining whether restrictions under the privatization regulations were implicated in the context of proposed sales of State-owned assets. She further explained that pursuant to the State Enterprises Management Entity definitions under privatization regulations, those regulations only apply to "Senior Managers," who are defined as an employee of a State-owned enterprise or an individual assigned by the government to work on behalf of a joint venture owned in part by the government. Based on the Requestor's representation that the Foreign Private Company Owner was the General Manager of the Investment Target, appointed as the minority-owner's representative, one staff member indicated that the Foreign Private Company Owner would not be considered a manager of sufficient authority to come within the privatization regulations because the Foreign Private Company Owner's position at the Investment Target did not convey any state or government status to him.[6] After reviewing the official State Enterprises Divestiture Entity files relating to the Investment Target tender, the staff member confirmed that the State Enterprises Divestiture Entity had explicitly determined that the privatization regulations do not apply to the Foreign Private Company Owner because he is not a

[5] The Investment Target Chairman further explained that the government's decision to divest its shares of the Investment Target was made by the State Enterprises Management Entity, and that the decision was approved by the Foreign Government Owner's board.

[6] She further explained that the seller – here the Foreign Government Owner – was required to identify the Senior Managers of the government-owned entity being sold in its tender application to the State Enterprises Divestiture Entity.

government official within the meaning of those regulations, despite his status as the General Manager of The Investment Target.[7] The supervisor in the State-Owned Asset Department of the State Enterprises Divestiture Entity, who was the contact person and coordinator of the Foreign Government Owner share sale, concurred with this interpretation of the privatization regulations. Subsequent to this meeting, the Requester sent a letter to one of the staff members reiterating the same basic disclosures noted above, and specifically confirming the State Enterprises Divestiture Entity's determination that the privatization regulations do not apply to the Foreign Private Company Owner.

Revised FCPA Considerations

Despite the initial FCPA risks identified by the Requestor, and the Foreign Private Company Owner's initial reluctance to make disclosures believed at that time necessary to alleviate those risks, based on the Requestor's original FCPA due diligence efforts together with its additional due diligence efforts described above, the Requestor has stated that it is prepared to proceed with the Proposed Transaction.

While the Requestor believes that the Foreign Private Company Owner is likely considered a "foreign official" under the FCPA, at least during the period when the Investment Target remains a government-owned entity and he is the General Manager of that entity, the Requestor notes and represents the following:

The Foreign Private Company Owner is purchasing the Investment Target shares without financial assistance from the Requestor. As represented by high-ranking officials at the State Enterprises Divestiture Entity, the Foreign Private Company Owner must provide the entirety of the funds required to purchase the Investment Target shares prior to finalization of the purchase. The Foreign Private Company Owner is in the process of doing so, through installment payments, without the assistance of the Requestor. A necessary and explicit predicate to the Requestor's participation in the Proposed Transaction is Foreign Private Company 2's full and legal ownership of 100% of the Investment Target. Thus, the Requestor will not close the Proposed Transaction until the Foreign Private Company Owner's purchase of the Foreign Government Owner's shares of the Investment Target shares is complete. Further, the Requestor has not made, and warrants that it will not make, any direct or indirect payment to the Foreign Private Company Owner to make possible his intended purchase of those shares.

The Requestor will make no extra or unjustified payments to the Foreign Private Company Owner. The Requestor confirms that it has not made any payments to the Foreign Private Company Owner to date. The Requestor further warrants that, in connection with the Proposed Transaction, it will not pay the Foreign Private Company Owner anything other than the agreed-

[7] The Requestor's outside counsel has consulted with attorneys in its office in the host country who have confirmed that the determination whether a manager of a State-controlled enterprise is a covered person under the privatization regulations is within the discretion of the State Enterprises Divestiture Entity.

upon purchase price for the Investment Target shares, and reasonable fees in connection with the Foreign Private Company Owner's actual involvement in the management of the Investment Target joint venture as set out in the final joint venture agreement. The Foreign Private Company Owner has also assured the Requestor that he will not use any payments from the Requestor to pay government officials, and the Foreign Private Company Owner will be required to guarantee as much within the documentation of the Proposed Transaction.

The Requestor will make no payments to any other foreign officials. The Requestor believes, after reasonable inquiry, that no investor of Foreign Private Company 2 from whom the Requestor would purchase shares in the Investment Target, with the exception of the Foreign Private Company Owner, is a foreign official. Moreover, after reasonable inquiry, no owner, officer, director, consultant, representative or agent of Foreign Private Company 2, or close relative of the Foreign Private Company Owner, is known to be a foreign official. Further, under the joint venture agreement, the Foreign Private Company Owner will be required to inform the Requestor of any instances where the government status of those individuals changes.

The premium between the Foreign Private Company Owner's purchase price of the Investment Target shares and the Requestor's purchase price is justified based on legitimate business considerations. The Requestor has confirmed through various due diligence efforts, including conversations with high-ranking State Enterprises Divestiture Entity officials, that: (1) the Foreign Private Company Owner's bid price for the Investment Target shares was appropriate; (2) valuation methodologies in the foreign country differ, sometimes dramatically, from American valuation methodologies in that the foreign country valuations often do not include future value calculations for assets such as the Investment Target shares; and thus, (3) the Requestor's valuation and purchase of the Investment Target shares at a substantial premium over the Foreign Private Company Owner's purchase price is justified based on legitimate business considerations.[8] Lastly, in connection with and as an essential condition of the Proposed Transaction, the Requestor is receiving valuable concessions in the revised joint venture agreement which include, but are not limited to, services and hardware supply contracts between the joint venture and the Requestor's foreign subsidiary, a preferred return, and effective control of the joint venture board and appointment of all senior management.

The Foreign Private Company Owner's status as a "foreign official" will soon cease. The Requestor believes that, upon finalization of the Foreign Private Company Owner's purchase of the Foreign Government Owner's shares of the Investment Target, the Foreign Private Company Owner could no longer be considered a "foreign official" under the FCPA. At that point, the Requestor understands that the Foreign Private Company Owner will have no formal or actual role with any government-owned entity, further decreasing any FCPA risk.

[8] Further to this point, the Requestor warrants that its valuation of the controlling interest in the Investment Target is based both on future anticipated revenue and profit streams from that investment and the significant derivative financial benefits associated with the acquisition of a competitively advantageous portion of the relevant regional public services market.

The Foreign Private Company Owner's purchase of the Foreign Government Owner's shares is lawful under the foreign country's laws. The Requestor has learned that the State Enterprises Divestiture Entity does not consider the Foreign Private Company Owner subject to the privatization regulations. This interpretation was stated orally (and confirmed by the Requestor in writing) by informed government officials specifically responsible for interpreting the privatization regulations, and appears to reflect the official State Enterprises Divestiture Entity determination on that issue. The conclusion apparently reflects the government's conclusion that the Foreign Private Company Owner is not a member of senior management for purposes of the privatization regulations and he does not otherwise have government official status by virtue of any other position he holds. The Requestor is not aware, after making reasonable inquiry, of any other formal connection between the Foreign Private Company Owner and the government aside from his current nominal role at the Investment Target. In light of these facts, the Foreign Private Company Owner's lack of practical control over any government entity, and the government's assertion that the Foreign Private Company Owner does not represent its interests, the Requestor is prepared to proceed with the Proposed Transaction.

In pursuing the Proposed Transaction, the Foreign Private Company Owner is not illegally or inappropriately acting on a corporate opportunity belonging to the joint venture. The State Enterprises Management Entity and the Foreign Government Owner made the decision to divest their shares in the Investment Target. As is required by law, the sale of State assets, in this case the shares in the Investment Target owned by the Foreign Government Owner, was conducted through the public tender process managed by the State Enterprises Divestiture Entity. Prior to concluding that transaction, the existence of the discussions between the Requestor and the Foreign Private Company Owner, his various roles and interests, and the details relating to the Proposed Transaction – including the fact that the Requestor was offering the Foreign Private Company Owner a substantial premium for a controlling interest in the Investment Target – were disclosed to high level officials at the State Enterprises Divestiture Entity and the Foreign Government Owner and its parent shareholders.

The State Enterprises Divestiture Entity officials also have been advised of the Proposed Transaction, including the fact that the Foreign Private Company Owner will receive from the Requestor a significant premium over the price at which he acquired the Investment Target, and such officials have expressed no reservations about the Foreign Private Company Owner's participation, the premium he is to receive from the Requestor on his shares, or otherwise. Even if the Foreign Private Company Owner was subject to the privatization regulations, disclosure has now been made to the relevant government entities. In particular, the Requestor explicitly informed high-ranking officials at the Investment Target, the Foreign Government Owner, and the State Enterprises Divestiture Entity that: (1) the Foreign Private Company Owner was the General Manager of the Investment Target; (2) the Foreign Private Company Owner was the ultimate beneficial owner of Foreign Private Company 1 and Foreign Private Company 2; and (3) the Foreign Private Company Owner, through Foreign Private Company 2, stood to receive a substantial price premium from the Requestor for a portion of his shares in the Investment Target. The government officials with whom the Requestor spoke expressed no reservations

about the propriety of the Foreign Private Company Owner's participation in and profit from the Proposed Transaction.

Due Diligence Documentation and Contractual Provisions

The Requestor has represented in its request that it has fully documented all of the due diligence it conducted with regard to the Proposed Transaction, and will maintain such documentation in the Requestor's offices in the United States.

The Requestor has further represented that the Foreign Private Company Owner, as Chairman, will provide a representation and warranty on behalf of Foreign Private Company 2 that: (1) neither Foreign Private Company 2 nor its owners, directors, officers, employees, agents, or close family members thereof, have made any payment directly or indirectly in violation of relevant anti-corruption laws, including the FCPA; (2) no payment will be made in the future in violation of relevant anti-corruption laws, including the FCPA; and (3) it has an ongoing obligation to comply with relevant anti-corruption laws. The Requestor has further represented that under its joint venture agreement with Foreign Private Company 2, the Requestor will have the right to withhold payments to Foreign Private Company 2 and/or terminate the joint venture agreement and dissolve the joint venture entity in the event of a breach of the agreement, including violations of relevant anti-corruption laws. In addition, the agreement will contain provisions providing for one party to buy out the other in the event of breach of the agreement.

Conclusion

Based upon all the facts and circumstances as represented by the Requestor, the Department does not presently intend to take any enforcement action with respect to the Proposed Transaction, a prospective majority investment by the Requestor in the Investment Target, an entity that would be responsible for providing certain public services to a municipality in the host country.

This determination is based on several important factors. First, the Requestor conducted and documented reasonable due diligence of the anticipated seller of privatized shares of the Investment Target, with attention to both FCPA risks and compliance with local laws and regulations, and will maintain such documentation in the United States. Second, the Requestor required and obtained transparency through adequate disclosures to the relevant government entities of the anticipated purchase at a significant premium from the Foreign Private Company Owner of the majority of shares in the Investment Target, following the Foreign Private Company Owner's completion of his purchase of the Foreign Government Owner's shares through the public tender process. Third, the Requestor will obtain from the Foreign Private Company Owner representations and warranties regarding past and future anti-corruption compliance. And fourth, the Requestor will retain the contractual rights to discontinue its business relationship with Foreign Private Company 2 in the event of breach of their joint venture agreement, including violations of anti-corruption laws.

This Opinion, however, is subject to the following important caveats: the FCPA Opinion Letter

and Release can be relied upon by you only to the extent that the disclosure of facts and circumstances in your Request is accurate and complete and remains accurate and complete. Additionally, this Opinion Letter and Release have no binding application on any party that did not join in the Request.

SCHEDULE D
COMPLIANCE CERTIFICATE

This certificate is delivered pursuant to Section 11.8 of the Distribution Agreement, dated as of _____, 2008 (the "Distribution Agreement"), among _____, a corporation organized under the laws of the State of _____, USA (the "Company"), and _____, a corporation organized under the laws of _____ (the "Distributor"). Any capitalized terms used herein, unless otherwise defined herein, shall have the meanings assigned to such terms in the Distribution Agreement.

I, _____ ***[insert name of certifying officer of Distributor]***, the _____ ***[insert title of certifying officer]*** of the Distributor, do hereby certify as follows:

I am the duly qualified and acting _____*[insert title of certifying officer]* of the Distributor, and as such I am familiar with the Distributor's business practices, accounting and records systems and I am qualified to certify the information contained herein. I hereby confirm that the Distributor and each of its sub-agents, sub-distributors, consultants, directors, officers, employees, agents and representatives have, for the twelve (12) month period ended December 31, 20___, complied in all respects with all applicable laws as required by the Distribution Agreement, including without limitation Sections 11.1, 11.2, 11.3, 11.4, 11.5, 11.6 and 11.7 of the Distribution Agreement.

IN WITNESS THEREOF, I have hereunto subscribed my name as of this _____ day of _____, 20___.

_____

Name:

Title:

Public Law 107–204
107th Congress

An Act

To protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws, and for other purposes.

July 30, 2002
[H.R. 3763]

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

Sarbanes-Oxley Act of 2002. Corporate responsibility. 15 USC 7201 note.

SECTION 1. SHORT TITLE; TABLE OF CONTENTS.

(a) SHORT TITLE.—This Act may be cited as the "Sarbanes-Oxley Act of 2002".

(b) TABLE OF CONTENTS.—The table of contents for this Act is as follows:

15 USC 7201.

SEC. 2. DEFINITIONS.

(a) IN GENERAL.—In this Act, the following definitions shall apply:

(1) APPROPRIATE STATE REGULATORY AUTHORITY.—The term "appropriate State regulatory authority" means the State agency or other authority responsible for the licensure or other regulation of the practice of accounting in the State or States having jurisdiction over a registered public accounting firm or associated person thereof, with respect to the matter in question.

(2) AUDIT.—The term "audit" means an examination of the financial statements of any issuer by an independent public accounting firm in accordance with the rules of the Board or the Commission (or, for the period preceding the adoption of applicable rules of the Board under section 103, in accordance with then-applicable generally accepted auditing and related standards for such purposes), for the purpose of expressing an opinion on such statements.

(3) AUDIT COMMITTEE.—The term "audit committee" means—

(A) a committee (or equivalent body) established by and amongst the board of directors of an issuer for the purpose of overseeing the accounting and financial reporting processes of the issuer and audits of the financial statements of the issuer; and

(B) if no such committee exists with respect to an issuer, the entire board of directors of the issuer.

(4) AUDIT REPORT.—The term "audit report" means a document or other record—

(A) prepared following an audit performed for purposes of compliance by an issuer with the requirements of the securities laws; and

(B) in which a public accounting firm either—

(i) sets forth the opinion of that firm regarding a financial statement, report, or other document; or

(ii) asserts that no such opinion can be expressed.

(5) BOARD.—The term "Board" means the Public Company Accounting Oversight Board established under section 101.

(6) COMMISSION.—The term "Commission" means the Securities and Exchange Commission.

(7) ISSUER.—The term "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) (15 U.S.C. 78o(d)), or that files or has filed 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.

(8) NON-AUDIT SERVICES.—The term "non-audit services" means any professional services provided to an issuer by a registered public accounting firm, other than those provided to an issuer in connection with an audit or a review of the financial statements of an issuer.

(9) PERSON ASSOCIATED WITH A PUBLIC ACCOUNTING FIRM.—

(A) IN GENERAL.—The terms "person associated with a public accounting firm" (or with a "registered public accounting firm") and "associated person of a public accounting firm" (or of a "registered public accounting firm") mean any individual proprietor, partner, shareholder, principal, accountant, or other professional employee of a public accounting firm, or any other independent contractor or entity that, in connection with the preparation or issuance of any audit report—

(i) shares in the profits of, or receives compensation in any other form from, that firm; or

(ii) participates as agent or otherwise on behalf of such accounting firm in any activity of that firm.

(B) EXEMPTION AUTHORITY.—The Board may, by rule, exempt persons engaged only in ministerial tasks from the definition in subparagraph (A), to the extent that the Board determines that any such exemption is consistent with the purposes of this Act, the public interest, or the protection of investors.

(10) PROFESSIONAL STANDARDS.—The term "professional standards" means—

(A) accounting principles that are—

(i) established by the standard setting body described in section 19(b) of the Securities Act of 1933, as amended by this Act, or prescribed by the Commission under section 19(a) of that Act (15 U.S.C. 17a(s)) or section 13(b) of the Securities Exchange Act of 1934 (15 U.S.C. 78a(m)); and

(ii) relevant to audit reports for particular issuers, or dealt with in the quality control system of a particular registered public accounting firm; and

(B) auditing standards, standards for attestation engagements, quality control policies and procedures, ethical and competency standards, and independence standards (including rules implementing title II) that the Board or the Commission determines—

(i) relate to the preparation or issuance of audit reports for issuers; and

(ii) are established or adopted by the Board under section 103(a), or are promulgated as rules of the Commission.

(11) PUBLIC ACCOUNTING FIRM.—The term "public accounting firm" means—

(A) a proprietorship, partnership, incorporated association, corporation, limited liability company, limited liability partnership, or other legal entity that is engaged in the practice of public accounting or preparing or issuing audit reports; and

(B) to the extent so designated by the rules of the Board, any associated person of any entity described in subparagraph (A).

(12) REGISTERED PUBLIC ACCOUNTING FIRM.—The term "registered public accounting firm" means a public accounting firm registered with the Board in accordance with this Act.

(13) RULES OF THE BOARD.—The term "rules of the Board" means the bylaws and rules of the Board (as submitted to, and approved, modified, or amended by the Commission, in accordance with section 107), and those stated policies, practices, and interpretations of the Board that the Commission, by rule, may deem to be rules of the Board, as necessary or appropriate in the public interest or for the protection of investors.

(14) SECURITY.—The term "security" has the same meaning as in section 3(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)).

(15) SECURITIES LAWS.—The term "securities laws" means the provisions of law referred to in section 3(a)(47) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(47)), as amended by this Act, and includes the rules, regulations, and orders issued by the Commission thereunder.

(16) STATE.—The term "State" means any State of the United States, the District of Columbia, Puerto Rico, the Virgin Islands, or any other territory or possession of the United States.

(b) CONFORMING AMENDMENT.—Section 3(a)(47) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(47)) is amended by inserting "the Sarbanes-Oxley Act of 2002," before "the Public".

SEC. 3. COMMISSION RULES AND ENFORCEMENT. 15 USC 7202.

(a) REGULATORY ACTION.—The Commission shall promulgate such rules and regulations, as may be necessary or appropriate in the public interest or for the protection of investors, and in furtherance of this Act.

(b) ENFORCEMENT.—

(1) IN GENERAL.—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 violation of the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) or the rules and regulations issued thereunder, consistent with the provisions of this Act, and any such person shall be subject to the same penalties, and to the same extent, as for a violation of that Act or such rules or regulations.

(2) INVESTIGATIONS, INJUNCTIONS, AND PROSECUTION OF OFFENSES.—Section 21 of the Securities Exchange Act of 1934 (15 U.S.C. 78u) is amended—

(A) in subsection (a)(1), by inserting "the rules of the Public Company Accounting Oversight Board, of which such person is a registered public accounting firm or a person associated with such a firm," after "is a participant,";

(B) in subsection (d)(1), by inserting "the rules of the Public Company Accounting Oversight Board, of which such person is a registered public accounting firm or a person associated with such a firm," after "is a participant,";

(C) in subsection (e), by inserting "the rules of the Public Company Accounting Oversight Board, of which such person is a registered public accounting firm or a person associated with such a firm," after "is a participant,"; and

(D) in subsection (f), by inserting "or the Public Company Accounting Oversight Board" after "self-regulatory organization" each place that term appears.

(3) CEASE-AND-DESIST PROCEEDINGS.—Section 21C(c)(2) of the Securities Exchange Act of 1934 (15 U.S.C. 78u–3(c)(2)) is amended by inserting "registered public accounting firm (as defined in section 2 of the Sarbanes-Oxley Act of 2002)," after "government securities dealer,".

(4) ENFORCEMENT BY FEDERAL BANKING AGENCIES.—Section 12(i) of the Securities Exchange Act of 1934 (15 U.S.C. 78l(i)) is amended by—

(A) striking "sections 12," each place it appears and inserting "sections 10A(m), 12,"; and

(B) striking "and 16," each place it appears and inserting "and 16 of this Act, and sections 302, 303, 304, 306, 401(b), 404, 406, and 407 of the Sarbanes-Oxley Act of 2002,".

(c) EFFECT ON COMMISSION AUTHORITY.—Nothing in this Act or the rules of the Board shall be construed to impair or limit—

(1) the authority of the Commission to regulate the accounting profession, accounting firms, or persons associated with such firms for purposes of enforcement of the securities laws;

(2) the authority of the Commission to set standards for accounting or auditing practices or auditor independence, derived from other provisions of the securities laws or the rules or regulations thereunder, for purposes of the preparation and issuance of any audit report, or otherwise under applicable law; or

(3) the ability of the Commission to take, on the initiative of the Commission, legal, administrative, or disciplinary action against any registered public accounting firm or any associated person thereof.

TITLE I—PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD

15 USC 7211.

SEC. 101. ESTABLISHMENT; ADMINISTRATIVE PROVISIONS.

(a) ESTABLISHMENT OF BOARD.—There is established the Public Company Accounting Oversight Board, to oversee the audit of public companies that are subject to the securities laws, and related matters, in order to protect the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports for companies the securities of which are sold to, and held by and for, public investors. The Board shall be a body corporate, operate as a nonprofit corporation, and have succession until dissolved by an Act of Congress.

(b) STATUS.—The Board shall not be an agency or establishment of the United States Government, and, except as otherwise provided in this Act, shall be subject to, and have all the powers conferred upon a nonprofit corporation by, the District of Columbia Nonprofit Corporation Act. No member or person employed by, or agent for, the Board shall be deemed to be an officer or employee of or agent for the Federal Government by reason of such service.

(c) DUTIES OF THE BOARD.—The Board shall, subject to action by the Commission under section 107, and once a determination is made by the Commission under subsection (d) of this section—

(1) register public accounting firms that prepare audit reports for issuers, in accordance with section 102;

(2) establish or adopt, or both, by rule, auditing, quality control, ethics, independence, and other standards relating to the preparation of audit reports for issuers, in accordance with section 103;

(3) conduct inspections of registered public accounting firms, in accordance with section 104 and the rules of the Board;

(4) conduct investigations and disciplinary proceedings concerning, and impose appropriate sanctions where justified upon,

registered public accounting firms and associated persons of such firms, in accordance with section 105;

(5) perform such other duties or functions as the Board (or the Commission, by rule or order) determines are necessary or appropriate to promote high professional standards among, and improve the quality of audit services offered by, registered public accounting firms and associated persons thereof, or otherwise to carry out this Act, in order to protect investors, or to further the public interest;

(6) enforce compliance with this Act, the rules of the Board, professional standards, and the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto, by registered public accounting firms and associated persons thereof; and

(7) set the budget and manage the operations of the Board and the staff of the Board.

(d) COMMISSION DETERMINATION.—The members of the Board shall take such action (including hiring of staff, proposal of rules, and adoption of initial and transitional auditing and other professional standards) as may be necessary or appropriate to enable the Commission to determine, not later than 270 days after the date of enactment of this Act, that the Board is so organized and has the capacity to carry out the requirements of this title, and to enforce compliance with this title by registered public accounting firms and associated persons thereof. The Commission shall be responsible, prior to the appointment of the Board, for the planning for the establishment and administrative transition to the Board's operation.

(e) BOARD MEMBERSHIP.—

(1) COMPOSITION.—The Board shall have 5 members, appointed from among prominent individuals of integrity and reputation who have a demonstrated commitment to the interests of investors and the public, and an understanding of the responsibilities for and nature of the financial disclosures required of issuers under the securities laws and the obligations of accountants with respect to the preparation and issuance of audit reports with respect to such disclosures.

(2) LIMITATION.—Two members, and only 2 members, of the Board shall be or have been certified public accountants pursuant to the laws of 1 or more States, provided that, if 1 of those 2 members is the chairperson, he or she may not have been a practicing certified public accountant for at least 5 years prior to his or her appointment to the Board.

(3) FULL-TIME INDEPENDENT SERVICE.—Each member of the Board shall serve on a full-time basis, and may not, concurrent with service on the Board, be employed by any other person or engage in any other professional or business activity. No member of the Board may share in any of the profits of, or receive payments from, a public accounting firm (or any other person, as determined by rule of the Commission), other than fixed continuing payments, subject to such conditions as the Commission may impose, under standard arrangements for the retirement of members of public accounting firms.

(4) APPOINTMENT OF BOARD MEMBERS.—

(A) INITIAL BOARD.—Not later than 90 days after the date of enactment of this Act, the Commission, after consultation with the Chairman of the Board of Governors

Deadline.

of the Federal Reserve System and the Secretary of the Treasury, shall appoint the chairperson and other initial members of the Board, and shall designate a term of service for each.

(B) VACANCIES.—A vacancy on the Board shall not affect the powers of the Board, but shall be filled in the same manner as provided for appointments under this section.

(5) TERM OF SERVICE.—

(A) IN GENERAL.—The term of service of each Board member shall be 5 years, and until a successor is appointed, except that—

(i) the terms of office of the initial Board members (other than the chairperson) shall expire in annual increments, 1 on each of the first 4 anniversaries of the initial date of appointment; and

(ii) any Board member appointed to fill a vacancy occurring before the expiration of the term for which the predecessor was appointed shall be appointed only for the remainder of that term.

(B) TERM LIMITATION.—No person may serve as a member of the Board, or as chairperson of the Board, for more than 2 terms, whether or not such terms of service are consecutive.

(6) REMOVAL FROM OFFICE.—A member of the Board may be removed by the Commission from office, in accordance with section 107(d)(3), for good cause shown before the expiration of the term of that member.

(f) POWERS OF THE BOARD.—In addition to any authority granted to the Board otherwise in this Act, the Board shall have the power, subject to section 107—

(1) to sue and be sued, complain and defend, in its corporate name and through its own counsel, with the approval of the Commission, in any Federal, State, or other court;

(2) to conduct its operations and maintain offices, and to exercise all other rights and powers authorized by this Act, in any State, without regard to any qualification, licensing, or other provision of law in effect in such State (or a political subdivision thereof);

(3) to lease, purchase, accept gifts or donations of or otherwise acquire, improve, use, sell, exchange, or convey, all of or an interest in any property, wherever situated;

(4) to appoint such employees, accountants, attorneys, and other agents as may be necessary or appropriate, and to determine their qualifications, define their duties, and fix their salaries or other compensation (at a level that is comparable to private sector self-regulatory, accounting, technical, supervisory, or other staff or management positions);

(5) to allocate, assess, and collect accounting support fees established pursuant to section 109, for the Board, and other fees and charges imposed under this title; and

Contracts.

(6) to enter into contracts, execute instruments, incur liabilities, and do any and all other acts and things necessary, appropriate, or incidental to the conduct of its operations and the exercise of its obligations, rights, and powers imposed or granted by this title.

(g) RULES OF THE BOARD.—The rules of the Board shall, subject to the approval of the Commission—

(1) provide for the operation and administration of the Board, the exercise of its authority, and the performance of its responsibilities under this Act;

(2) permit, as the Board determines necessary or appropriate, delegation by the Board of any of its functions to an individual member or employee of the Board, or to a division of the Board, including functions with respect to hearing, determining, ordering, certifying, reporting, or otherwise acting as to any matter, except that—

(A) the Board shall retain a discretionary right to review any action pursuant to any such delegated function, upon its own motion;

(B) a person shall be entitled to a review by the Board with respect to any matter so delegated, and the decision of the Board upon such review shall be deemed to be the action of the Board for all purposes (including appeal or review thereof); and

(C) if the right to exercise a review described in subparagraph (A) is declined, or if no such review is sought within the time stated in the rules of the Board, then the action taken by the holder of such delegation shall for all purposes, including appeal or review thereof, be deemed to be the action of the Board;

(3) establish ethics rules and standards of conduct for Board members and staff, including a bar on practice before the Board (and the Commission, with respect to Board-related matters) of 1 year for former members of the Board, and appropriate periods (not to exceed 1 year) for former staff of the Board; and

(4) provide as otherwise required by this Act.

(h) ANNUAL REPORT TO THE COMMISSION.—The Board shall submit an annual report (including its audited financial statements) to the Commission, and the Commission shall transmit a copy of that report to the Committee on Banking, Housing, and Urban Affairs of the Senate, and the Committee on Financial Services of the House of Representatives, not later than 30 days after the date of receipt of that report by the Commission.

Deadline.

SEC. 102. REGISTRATION WITH THE BOARD.

15 USC 7212.

(a) MANDATORY REGISTRATION.—Beginning 180 days after the date of the determination of the Commission under section 101(d), it shall be unlawful for any person that is not a registered public accounting firm to prepare or issue, or to participate in the preparation or issuance of, any audit report with respect to any issuer.

(b) APPLICATIONS FOR REGISTRATION.—

(1) FORM OF APPLICATION.—A public accounting firm shall use such form as the Board may prescribe, by rule, to apply for registration under this section.

(2) CONTENTS OF APPLICATIONS.—Each public accounting firm shall submit, as part of its application for registration, in such detail as the Board shall specify—

(A) the names of all issuers for which the firm prepared or issued audit reports during the immediately preceding calendar year, and for which the firm expects to prepare or issue audit reports during the current calendar year;

(B) the annual fees received by the firm from each such issuer for audit services, other accounting services, and non-audit services, respectively;

(C) such other current financial information for the most recently completed fiscal year of the firm as the Board may reasonably request;

(D) a statement of the quality control policies of the firm for its accounting and auditing practices;

(E) a list of all accountants associated with the firm who participate in or contribute to the preparation of audit reports, stating the license or certification number of each such person, as well as the State license numbers of the firm itself;

(F) information relating to criminal, civil, or administrative actions or disciplinary proceedings pending against the firm or any associated person of the firm in connection with any audit report;

(G) copies of any periodic or annual disclosure filed by an issuer with the Commission during the immediately preceding calendar year which discloses accounting disagreements between such issuer and the firm in connection with an audit report furnished or prepared by the firm for such issuer; and

(H) such other information as the rules of the Board or the Commission shall specify as necessary or appropriate in the public interest or for the protection of investors.

(3) CONSENTS.—Each application for registration under this subsection shall include—

(A) a consent executed by the public accounting firm to cooperation in and compliance with any request for testimony or the production of documents made by the Board in the furtherance of its authority and responsibilities under this title (and an agreement to secure and enforce similar consents from each of the associated persons of the public accounting firm as a condition of their continued employment by or other association with such firm); and

(B) a statement that such firm understands and agrees that cooperation and compliance, as described in the consent required by subparagraph (A), and the securing and enforcement of such consents from its associated persons, in accordance with the rules of the Board, shall be a condition to the continuing effectiveness of the registration of the firm with the Board.

(c) ACTION ON APPLICATIONS.—

Deadline.

(1) TIMING.—The Board shall approve a completed application for registration not later than 45 days after the date of receipt of the application, in accordance with the rules of the Board, unless the Board, prior to such date, issues a written notice of disapproval to, or requests more information from, the prospective registrant.

(2) TREATMENT.—A written notice of disapproval of a completed application under paragraph (1) for registration shall be treated as a disciplinary sanction for purposes of sections 105(d) and 107(c).

(d) PERIODIC REPORTS.—Each registered public accounting firm shall submit an annual report to the Board, and may be required to report more frequently, as necessary to update the information contained in its application for registration under this section, and to provide to the Board such additional information as the Board or the Commission may specify, in accordance with subsection (b)(2).

(e) PUBLIC AVAILABILITY.—Registration applications and annual reports required by this subsection, or such portions of such applications or reports as may be designated under rules of the Board, shall be made available for public inspection, subject to rules of the Board or the Commission, and to applicable laws relating to the confidentiality of proprietary, personal, or other information contained in such applications or reports, provided that, in all events, the Board shall protect from public disclosure information reasonably identified by the subject accounting firm as proprietary information.

(f) REGISTRATION AND ANNUAL FEES.—The Board shall assess and collect a registration fee and an annual fee from each registered public accounting firm, in amounts that are sufficient to recover the costs of processing and reviewing applications and annual reports.

SEC. 103. AUDITING, QUALITY CONTROL, AND INDEPENDENCE STANDARDS AND RULES.

15 USC 7213.

(a) AUDITING, QUALITY CONTROL, AND ETHICS STANDARDS.—

(1) IN GENERAL.—The Board shall, by rule, establish, including, to the extent it determines appropriate, through adoption of standards proposed by 1 or more professional groups of accountants designated pursuant to paragraph (3)(A) or advisory groups convened pursuant to paragraph (4), and amend or otherwise modify or alter, such auditing and related attestation standards, such quality control standards, and such ethics standards to be used by registered public accounting firms in the preparation and issuance of audit reports, as required by this Act or the rules of the Commission, or as may be necessary or appropriate in the public interest or for the protection of investors.

(2) RULE REQUIREMENTS.—In carrying out paragraph (1), the Board—

(A) shall include in the auditing standards that it adopts, requirements that each registered public accounting firm shall—

(i) prepare, and maintain for a period of not less than 7 years, audit work papers, and other information related to any audit report, in sufficient detail to support the conclusions reached in such report;

(ii) provide a concurring or second partner review and approval of such audit report (and other related information), and concurring approval in its issuance, by a qualified person (as prescribed by the Board) associated with the public accounting firm, other than the person in charge of the audit, or by an independent reviewer (as prescribed by the Board); and

(iii) describe in each audit report the scope of the auditor's testing of the internal control structure and procedures of the issuer, required by section 404(b), and present (in such report or in a separate report)—

(I) the findings of the auditor from such testing;

(II) an evaluation of whether such internal control structure and procedures—

(aa) include maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the issuer;

(bb) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the issuer are being made only in accordance with authorizations of management and directors of the issuer; and

(III) a description, at a minimum, of material weaknesses in such internal controls, and of any material noncompliance found on the basis of such testing.

(B) shall include, in the quality control standards that it adopts with respect to the issuance of audit reports, requirements for every registered public accounting firm relating to—

(i) monitoring of professional ethics and independence from issuers on behalf of which the firm issues audit reports;

(ii) consultation within such firm on accounting and auditing questions;

(iii) supervision of audit work;

(iv) hiring, professional development, and advancement of personnel;

(v) the acceptance and continuation of engagements;

(vi) internal inspection; and

(vii) such other requirements as the Board may prescribe, subject to subsection (a)(1).

(3) AUTHORITY TO ADOPT OTHER STANDARDS.—

(A) IN GENERAL.—In carrying out this subsection, the Board—

(i) may adopt as its rules, subject to the terms of section 107, any portion of any statement of auditing standards or other professional standards that the Board determines satisfy the requirements of paragraph (1), and that were proposed by 1 or more professional groups of accountants that shall be designated or recognized by the Board, by rule, for such purpose, pursuant to this paragraph or 1 or more advisory groups convened pursuant to paragraph (4); and

(ii) notwithstanding clause (i), shall retain full authority to modify, supplement, revise, or subsequently amend, modify, or repeal, in whole or in part, any portion of any statement described in clause (i).

(B) INITIAL AND TRANSITIONAL STANDARDS.—The Board shall adopt standards described in subparagraph (A)(i) as initial or transitional standards, to the extent the Board determines necessary, prior to a determination of the Commission under section 101(d), and such standards shall be separately approved by the Commission at the time of that determination, without regard to the procedures required by section 107 that otherwise would apply to the approval of rules of the Board.

(4) ADVISORY GROUPS.—The Board shall convene, or authorize its staff to convene, such expert advisory groups as may be appropriate, which may include practicing accountants and other experts, as well as representatives of other interested groups, subject to such rules as the Board may prescribe to prevent conflicts of interest, to make recommendations concerning the content (including proposed drafts) of auditing, quality control, ethics, independence, or other standards required to be established under this section.

(b) INDEPENDENCE STANDARDS AND RULES.—The Board shall establish such rules as may be necessary or appropriate in the public interest or for the protection of investors, to implement, or as authorized under, title II of this Act.

(c) COOPERATION WITH DESIGNATED PROFESSIONAL GROUPS OF ACCOUNTANTS AND ADVISORY GROUPS.—

(1) IN GENERAL.—The Board shall cooperate on an ongoing basis with professional groups of accountants designated under subsection (a)(3)(A) and advisory groups convened under subsection (a)(4) in the examination of the need for changes in any standards subject to its authority under subsection (a), recommend issues for inclusion on the agendas of such designated professional groups of accountants or advisory groups, and take such other steps as it deems appropriate to increase the effectiveness of the standard setting process.

(2) BOARD RESPONSES.—The Board shall respond in a timely fashion to requests from designated professional groups of accountants and advisory groups referred to in paragraph (1) for any changes in standards over which the Board has authority.

(d) EVALUATION OF STANDARD SETTING PROCESS.—The Board shall include in the annual report required by section 101(h) the results of its standard setting responsibilities during the period to which the report relates, including a discussion of the work of the Board with any designated professional groups of accountants and advisory groups described in paragraphs (3)(A) and (4) of subsection (a), and its pending issues agenda for future standard setting projects.

SEC. 104. INSPECTIONS OF REGISTERED PUBLIC ACCOUNTING FIRMS. 15 USC 7214.

(a) IN GENERAL.—The Board shall conduct a continuing program of inspections to assess the degree of compliance of each registered public accounting firm and associated persons of that firm with this Act, the rules of the Board, the rules of the Commission, or professional standards, in connection with its performance of audits, issuance of audit reports, and related matters involving issuers.

(b) INSPECTION FREQUENCY.—

(1) IN GENERAL.—Subject to paragraph (2), inspections required by this section shall be conducted—

(A) annually with respect to each registered public accounting firm that regularly provides audit reports for more than 100 issuers; and

(B) not less frequently than once every 3 years with respect to each registered public accounting firm that regularly provides audit reports for 100 or fewer issuers.

(2) ADJUSTMENTS TO SCHEDULES.—The Board may, by rule, adjust the inspection schedules set under paragraph (1) if the Board finds that different inspection schedules are consistent with the purposes of this Act, the public interest, and the protection of investors. The Board may conduct special inspections at the request of the Commission or upon its own motion.

(c) PROCEDURES.—The Board shall, in each inspection under this section, and in accordance with its rules for such inspections—

(1) identify any act or practice or omission to act by the registered public accounting firm, or by any associated person thereof, revealed by such inspection that may be in violation of this Act, the rules of the Board, the rules of the Commission, the firm's own quality control policies, or professional standards;

(2) report any such act, practice, or omission, if appropriate, to the Commission and each appropriate State regulatory authority; and

(3) begin a formal investigation or take disciplinary action, if appropriate, with respect to any such violation, in accordance with this Act and the rules of the Board.

(d) CONDUCT OF INSPECTIONS.—In conducting an inspection of a registered public accounting firm under this section, the Board shall—

(1) inspect and review selected audit and review engagements of the firm (which may include audit engagements that are the subject of ongoing litigation or other controversy between the firm and 1 or more third parties), performed at various offices and by various associated persons of the firm, as selected by the Board;

(2) evaluate the sufficiency of the quality control system of the firm, and the manner of the documentation and communication of that system by the firm; and

(3) perform such other testing of the audit, supervisory, and quality control procedures of the firm as are necessary or appropriate in light of the purpose of the inspection and the responsibilities of the Board.

(e) RECORD RETENTION.—The rules of the Board may require the retention by registered public accounting firms for inspection purposes of records whose retention is not otherwise required by section 103 or the rules issued thereunder.

(f) PROCEDURES FOR REVIEW.—The rules of the Board shall provide a procedure for the review of and response to a draft inspection report by the registered public accounting firm under inspection. The Board shall take such action with respect to such response as it considers appropriate (including revising the draft report or continuing or supplementing its inspection activities before issuing a final report), but the text of any such response, appropriately redacted to protect information reasonably identified by the accounting firm as confidential, shall be attached to and made part of the inspection report.

(g) REPORT.—A written report of the findings of the Board for each inspection under this section, subject to subsection (h), shall be—

(1) transmitted, in appropriate detail, to the Commission and each appropriate State regulatory authority, accompanied by any letter or comments by the Board or the inspector, and any letter of response from the registered public accounting firm; and

(2) made available in appropriate detail to the public (subject to section 105(b)(5)(A), and to the protection of such confidential and proprietary information as the Board may determine to be appropriate, or as may be required by law), except that no portions of the inspection report that deal with criticisms of or potential defects in the quality control systems of the firm under inspection shall be made public if those criticisms or defects are addressed by the firm, to the satisfaction of the Board, not later than 12 months after the date of the inspection report.

(h) INTERIM COMMISSION REVIEW.—

(1) REVIEWABLE MATTERS.—A registered public accounting firm may seek review by the Commission, pursuant to such rules as the Commission shall promulgate, if the firm—

(A) has provided the Board with a response, pursuant to rules issued by the Board under subsection (f), to the substance of particular items in a draft inspection report, and disagrees with the assessments contained in any final report prepared by the Board following such response; or

(B) disagrees with the determination of the Board that criticisms or defects identified in an inspection report have not been addressed to the satisfaction of the Board within 12 months of the date of the inspection report, for purposes of subsection (g)(2).

(2) TREATMENT OF REVIEW.—Any decision of the Commission with respect to a review under paragraph (1) shall not be reviewable under section 25 of the Securities Exchange Act of 1934 (15 U.S.C. 78y), or deemed to be "final agency action" for purposes of section 704 of title 5, United States Code.

(3) TIMING.—Review under paragraph (1) may be sought during the 30-day period following the date of the event giving rise to the review under subparagraph (A) or (B) of paragraph (1).

SEC. 105. INVESTIGATIONS AND DISCIPLINARY PROCEEDINGS. 15 USC 7215.

(a) IN GENERAL.—The Board shall establish, by rule, subject to the requirements of this section, fair procedures for the investigation and disciplining of registered public accounting firms and associated persons of such firms. Establishment.

(b) INVESTIGATIONS.—

(1) AUTHORITY.—In accordance with the rules of the Board, the Board may conduct an investigation of any act or practice, or omission to act, by a registered public accounting firm, any associated person of such firm, or both, that may violate any provision of this Act, the rules of the Board, the provisions of the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto, including the rules of the Commission issued under this Act, or professional standards, regardless of how the act, practice, or omission is brought to the attention of the Board.

(2) TESTIMONY AND DOCUMENT PRODUCTION.—In addition to such other actions as the Board determines to be necessary or appropriate, the rules of the Board may—

(A) require the testimony of the firm or of any person associated with a registered public accounting firm, with respect to any matter that the Board considers relevant or material to an investigation;

(B) require the production of audit work papers and any other document or information in the possession of a registered public accounting firm or any associated person thereof, wherever domiciled, that the Board considers relevant or material to the investigation, and may inspect the books and records of such firm or associated person to verify the accuracy of any documents or information supplied;

(C) request the testimony of, and production of any document in the possession of, any other person, including any client of a registered public accounting firm that the Board considers relevant or material to an investigation under this section, with appropriate notice, subject to the needs of the investigation, as permitted under the rules of the Board; and

(D) provide for procedures to seek issuance by the Commission, in a manner established by the Commission, of a subpoena to require the testimony of, and production of any document in the possession of, any person, including any client of a registered public accounting firm, that the Board considers relevant or material to an investigation under this section.

(3) NONCOOPERATION WITH INVESTIGATIONS.—

(A) IN GENERAL.—If a registered public accounting firm or any associated person thereof refuses to testify, produce documents, or otherwise cooperate with the Board in connection with an investigation under this section, the Board may—

(i) suspend or bar such person from being associated with a registered public accounting firm, or require the registered public accounting firm to end such association;

(ii) suspend or revoke the registration of the public accounting firm; and

(iii) invoke such other lesser sanctions as the Board considers appropriate, and as specified by rule of the Board.

(B) PROCEDURE.—Any action taken by the Board under this paragraph shall be subject to the terms of section 107(c).

(4) COORDINATION AND REFERRAL OF INVESTIGATIONS.—

Notification.

(A) COORDINATION.—The Board shall notify the Commission of any pending Board investigation involving a potential violation of the securities laws, and thereafter coordinate its work with the work of the Commission's Division of Enforcement, as necessary to protect an ongoing Commission investigation.

(B) REFERRAL.—The Board may refer an investigation under this section—

(i) to the Commission;

(ii) to any other Federal functional regulator (as defined in section 509 of the Gramm-Leach-Bliley Act (15 U.S.C. 6809)), in the case of an investigation that concerns an audit report for an institution that is subject to the jurisdiction of such regulator; and

(iii) at the direction of the Commission, to—

(I) the Attorney General of the United States;

(II) the attorney general of 1 or more States; and

(III) the appropriate State regulatory authority.

(5) USE OF DOCUMENTS.—

(A) CONFIDENTIALITY.—Except as provided in subparagraph (B), all documents and information prepared or received by or specifically for the Board, and deliberations of the Board and its employees and agents, in connection with an inspection under section 104 or with an investigation under this section, shall be confidential and privileged as an evidentiary matter (and shall not be subject to civil discovery or other legal process) in any proceeding in any Federal or State court or administrative agency, and shall be exempt from disclosure, in the hands of an agency or establishment of the Federal Government, under the Freedom of Information Act (5 U.S.C. 552a), or otherwise, unless and until presented in connection with a public proceeding or released in accordance with subsection (c).

(B) AVAILABILITY TO GOVERNMENT AGENCIES.—Without the loss of its status as confidential and privileged in the hands of the Board, all information referred to in subparagraph (A) may—

(i) be made available to the Commission; and

(ii) in the discretion of the Board, when determined by the Board to be necessary to accomplish the purposes of this Act or to protect investors, be made available to—

(I) the Attorney General of the United States;

(II) the appropriate Federal functional regulator (as defined in section 509 of the Gramm-Leach-Bliley Act (15 U.S.C. 6809)), other than the Commission, with respect to an audit report for an institution subject to the jurisdiction of such regulator;

(III) State attorneys general in connection with any criminal investigation; and

(IV) any appropriate State regulatory authority,

each of which shall maintain such information as confidential and privileged.

(6) IMMUNITY.—Any employee of the Board engaged in carrying out an investigation under this Act shall be immune from any civil liability arising out of such investigation in the same manner and to the same extent as an employee of the Federal Government in similar circumstances.

(c) DISCIPLINARY PROCEDURES.—

(1) NOTIFICATION; RECORDKEEPING.—The rules of the Board shall provide that in any proceeding by the Board to determine

whether a registered public accounting firm, or an associated person thereof, should be disciplined, the Board shall—

(A) bring specific charges with respect to the firm or associated person;

(B) notify such firm or associated person of, and provide to the firm or associated person an opportunity to defend against, such charges; and

(C) keep a record of the proceedings.

(2) PUBLIC HEARINGS.—Hearings under this section shall not be public, unless otherwise ordered by the Board for good cause shown, with the consent of the parties to such hearing.

(3) SUPPORTING STATEMENT.—A determination by the Board to impose a sanction under this subsection shall be supported by a statement setting forth—

(A) each act or practice in which the registered public accounting firm, or associated person, has engaged (or omitted to engage), or that forms a basis for all or a part of such sanction;

(B) the specific provision of this Act, the securities laws, the rules of the Board, or professional standards which the Board determines has been violated; and

(C) the sanction imposed, including a justification for that sanction.

(4) SANCTIONS.—If the Board finds, based on all of the facts and circumstances, that a registered public accounting firm or associated person thereof has engaged in any act or practice, or omitted to act, in violation of this Act, the rules of the Board, the provisions of the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto, including the rules of the Commission issued under this Act, or professional standards, the Board may impose such disciplinary or remedial sanctions as it determines appropriate, subject to applicable limitations under paragraph (5), including—

(A) temporary suspension or permanent revocation of registration under this title;

(B) temporary or permanent suspension or bar of a person from further association with any registered public accounting firm;

(C) temporary or permanent limitation on the activities, functions, or operations of such firm or person (other than in connection with required additional professional education or training);

(D) a civil money penalty for each such violation, in an amount equal to—

(i) not more than $100,000 for a natural person or $2,000,000 for any other person; and

(ii) in any case to which paragraph (5) applies, not more than $750,000 for a natural person or $15,000,000 for any other person;

(E) censure;

(F) required additional professional education or training; or

(G) any other appropriate sanction provided for in the rules of the Board.

(5) INTENTIONAL OR OTHER KNOWING CONDUCT.—The sanctions and penalties described in subparagraphs (A) through (C) and (D)(ii) of paragraph (4) shall only apply to—

(A) intentional or knowing conduct, including reckless conduct, that results in violation of the applicable statutory, regulatory, or professional standard; or

(B) repeated instances of negligent conduct, each resulting in a violation of the applicable statutory, regulatory, or professional standard.

(6) FAILURE TO SUPERVISE.—

(A) IN GENERAL.—The Board may impose sanctions under this section on a registered accounting firm or upon the supervisory personnel of such firm, if the Board finds that—

(i) the firm has failed reasonably to supervise an associated person, either as required by the rules of the Board relating to auditing or quality control standards, or otherwise, with a view to preventing violations of this Act, the rules of the Board, the provisions of the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto, including the rules of the Commission under this Act, or professional standards; and

(ii) such associated person commits a violation of this Act, or any of such rules, laws, or standards.

(B) RULE OF CONSTRUCTION.—No associated person of a registered public accounting firm shall be deemed to have failed reasonably to supervise any other person for purposes of subparagraph (A), if—

(i) there have been established in and for that firm procedures, and a system for applying such procedures, that comply with applicable rules of the Board and that would reasonably be expected to prevent and detect any such violation by such associated person; and

(ii) such person has reasonably discharged the duties and obligations incumbent upon that person by reason of such procedures and system, and had no reasonable cause to believe that such procedures and system were not being complied with.

(7) EFFECT OF SUSPENSION.—

(A) ASSOCIATION WITH A PUBLIC ACCOUNTING FIRM.—It shall be unlawful for any person that is suspended or barred from being associated with a registered public accounting firm under this subsection willfully to become or remain associated with any registered public accounting firm, or for any registered public accounting firm that knew, or, in the exercise of reasonable care should have known, of the suspension or bar, to permit such an association, without the consent of the Board or the Commission.

(B) ASSOCIATION WITH AN ISSUER.—It shall be unlawful for any person that is suspended or barred from being associated with an issuer under this subsection willfully to become or remain associated with any issuer in an accountancy or a financial management capacity, and for any issuer that knew, or in the exercise of reasonable

care should have known, of such suspension or bar, to permit such an association, without the consent of the Board or the Commission.

(d) REPORTING OF SANCTIONS.—

(1) RECIPIENTS.—If the Board imposes a disciplinary sanction, in accordance with this section, the Board shall report the sanction to—

(A) the Commission;

(B) any appropriate State regulatory authority or any foreign accountancy licensing board with which such firm or person is licensed or certified; and

(C) the public (once any stay on the imposition of such sanction has been lifted).

(2) CONTENTS.—The information reported under paragraph (1) shall include—

(A) the name of the sanctioned person;

(B) a description of the sanction and the basis for its imposition; and

(C) such other information as the Board deems appropriate.

(e) STAY OF SANCTIONS.—

(1) IN GENERAL.—Application to the Commission for review, or the institution by the Commission of review, of any disciplinary action of the Board shall operate as a stay of any such disciplinary action, unless and until the Commission orders (summarily or after notice and opportunity for hearing on the question of a stay, which hearing may consist solely of the submission of affidavits or presentation of oral arguments) that no such stay shall continue to operate.

(2) EXPEDITED PROCEDURES.—The Commission shall establish for appropriate cases an expedited procedure for consideration and determination of the question of the duration of a stay pending review of any disciplinary action of the Board under this subsection.

15 USC 7216.

SEC. 106. FOREIGN PUBLIC ACCOUNTING FIRMS.

(a) APPLICABILITY TO CERTAIN FOREIGN FIRMS.—

(1) IN GENERAL.—Any foreign public accounting firm that prepares or furnishes an audit report with respect to any issuer, shall be subject to this Act and the rules of the Board and the Commission issued under this Act, in the same manner and to the same extent as a public accounting firm that is organized and operates under the laws of the United States or any State, except that registration pursuant to section 102 shall not by itself provide a basis for subjecting such a foreign public accounting firm to the jurisdiction of the Federal or State courts, other than with respect to controversies between such firms and the Board.

(2) BOARD AUTHORITY.—The Board may, by rule, determine that a foreign public accounting firm (or a class of such firms) that does not issue audit reports nonetheless plays such a substantial role in the preparation and furnishing of such reports for particular issuers, that it is necessary or appropriate, in light of the purposes of this Act and in the public interest or for the protection of investors, that such firm (or class of firms) should be treated as a public accounting firm

(or firms) for purposes of registration under, and oversight by the Board in accordance with, this title.

(b) PRODUCTION OF AUDIT WORKPAPERS.—

(1) CONSENT BY FOREIGN FIRMS.—If a foreign public accounting firm issues an opinion or otherwise performs material services upon which a registered public accounting firm relies in issuing all or part of any audit report or any opinion contained in an audit report, that foreign public accounting firm shall be deemed to have consented—

(A) to produce its audit workpapers for the Board or the Commission in connection with any investigation by either body with respect to that audit report; and

(B) to be subject to the jurisdiction of the courts of the United States for purposes of enforcement of any request for production of such workpapers.

(2) CONSENT BY DOMESTIC FIRMS.—A registered public accounting firm that relies upon the opinion of a foreign public accounting firm, as described in paragraph (1), shall be deemed—

(A) to have consented to supplying the audit workpapers of that foreign public accounting firm in response to a request for production by the Board or the Commission; and

(B) to have secured the agreement of that foreign public accounting firm to such production, as a condition of its reliance on the opinion of that foreign public accounting firm.

(c) EXEMPTION AUTHORITY.—The Commission, and the Board, subject to the approval of the Commission, may, by rule, regulation, or order, and as the Commission (or Board) determines necessary or appropriate in the public interest or for the protection of investors, either unconditionally or upon specified terms and conditions exempt any foreign public accounting firm, or any class of such firms, from any provision of this Act or the rules of the Board or the Commission issued under this Act.

(d) DEFINITION.—In this section, the term "foreign public accounting firm" means a public accounting firm that is organized and operates under the laws of a foreign government or political subdivision thereof.

SEC. 107. COMMISSION OVERSIGHT OF THE BOARD. 15 USC 7217.

(a) GENERAL OVERSIGHT RESPONSIBILITY.—The Commission shall have oversight and enforcement authority over the Board, as provided in this Act. The provisions of section 17(a)(1) of the Securities Exchange Act of 1934 (15 U.S.C. 78q(a)(1)), and of section 17(b)(1) of the Securities Exchange Act of 1934 (15 U.S.C. 78q(b)(1)) shall apply to the Board as fully as if the Board were a "registered securities association" for purposes of those sections 17(a)(1) and 17(b)(1).

(b) RULES OF THE BOARD.—

(1) DEFINITION.—In this section, the term "proposed rule" means any proposed rule of the Board, and any modification of any such rule.

(2) PRIOR APPROVAL REQUIRED.—No rule of the Board shall become effective without prior approval of the Commission in accordance with this section, other than as provided in section 103(a)(3)(B) with respect to initial or transitional standards.

(3) APPROVAL CRITERIA.—The Commission shall approve a proposed rule, if it finds that the rule is consistent with the requirements of this Act and the securities laws, or is necessary or appropriate in the public interest or for the protection of investors.

(4) PROPOSED RULE PROCEDURES.—The provisions of paragraphs (1) through (3) of section 19(b) of the Securities Exchange Act of 1934 (15 U.S.C. 78s(b)) shall govern the proposed rules of the Board, as fully as if the Board were a "registered securities association" for purposes of that section 19(b), except that, for purposes of this paragraph—

(A) the phrase "consistent with the requirements of this title and the rules and regulations thereunder applicable to such organization" in section 19(b)(2) of that Act shall be deemed to read "consistent with the requirements of title I of the Sarbanes-Oxley Act of 2002, and the rules and regulations issued thereunder applicable to such organization, or as necessary or appropriate in the public interest or for the protection of investors"; and

(B) the phrase "otherwise in furtherance of the purposes of this title" in section 19(b)(3)(C) of that Act shall be deemed to read "otherwise in furtherance of the purposes of title I of the Sarbanes-Oxley Act of 2002".

(5) COMMISSION AUTHORITY TO AMEND RULES OF THE BOARD.—The provisions of section 19(c) of the Securities Exchange Act of 1934 (15 U.S.C. 78s(c)) shall govern the abrogation, deletion, or addition to portions of the rules of the Board by the Commission as fully as if the Board were a "registered securities association" for purposes of that section 19(c), except that the phrase "to conform its rules to the requirements of this title and the rules and regulations thereunder applicable to such organization, or otherwise in furtherance of the purposes of this title" in section 19(c) of that Act shall, for purposes of this paragraph, be deemed to read "to assure the fair administration of the Public Company Accounting Oversight Board, conform the rules promulgated by that Board to the requirements of title I of the Sarbanes-Oxley Act of 2002, or otherwise further the purposes of that Act, the securities laws, and the rules and regulations thereunder applicable to that Board".

(c) COMMISSION REVIEW OF DISCIPLINARY ACTION TAKEN BY THE BOARD.—

(1) NOTICE OF SANCTION.—The Board shall promptly file notice with the Commission of any final sanction on any registered public accounting firm or on any associated person thereof, in such form and containing such information as the Commission, by rule, may prescribe.

(2) REVIEW OF SANCTIONS.—The provisions of sections 19(d)(2) and 19(e)(1) of the Securities Exchange Act of 1934 (15 U.S.C. 78s (d)(2) and (e)(1)) shall govern the review by the Commission of final disciplinary sanctions imposed by the Board (including sanctions imposed under section 105(b)(3) of this Act for noncooperation in an investigation of the Board), as fully as if the Board were a self-regulatory organization and the Commission were the appropriate regulatory agency for such organization for purposes of those sections 19(d)(2) and 19(e)(1), except that, for purposes of this paragraph—

(A) section 105(e) of this Act (rather than that section 19(d)(2)) shall govern the extent to which application for, or institution by the Commission on its own motion of, review of any disciplinary action of the Board operates as a stay of such action;

(B) references in that section 19(e)(1) to "members" of such an organization shall be deemed to be references to registered public accounting firms;

(C) the phrase "consistent with the purposes of this title" in that section 19(e)(1) shall be deemed to read "consistent with the purposes of this title and title I of the Sarbanes-Oxley Act of 2002";

(D) references to rules of the Municipal Securities Rulemaking Board in that section 19(e)(1) shall not apply; and

(E) the reference to section 19(e)(2) of the Securities Exchange Act of 1934 shall refer instead to section 107(c)(3) of this Act.

(3) COMMISSION MODIFICATION AUTHORITY.—The Commission may enhance, modify, cancel, reduce, or require the remission of a sanction imposed by the Board upon a registered public accounting firm or associated person thereof, if the Commission, having due regard for the public interest and the protection of investors, finds, after a proceeding in accordance with this subsection, that the sanction—

(A) is not necessary or appropriate in furtherance of this Act or the securities laws; or

(B) is excessive, oppressive, inadequate, or otherwise not appropriate to the finding or the basis on which the sanction was imposed.

(d) CENSURE OF THE BOARD; OTHER SANCTIONS.—

(1) RESCISSION OF BOARD AUTHORITY.—The Commission, by rule, consistent with the public interest, the protection of investors, and the other purposes of this Act and the securities laws, may relieve the Board of any responsibility to enforce compliance with any provision of this Act, the securities laws, the rules of the Board, or professional standards.

(2) CENSURE OF THE BOARD; LIMITATIONS.—The Commission may, by order, as it determines necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this Act or the securities laws, censure or impose limitations upon the activities, functions, and operations of the Board, if the Commission finds, on the record, after notice and opportunity for a hearing, that the Board—

(A) has violated or is unable to comply with any provision of this Act, the rules of the Board, or the securities laws; or

(B) without reasonable justification or excuse, has failed to enforce compliance with any such provision or rule, or any professional standard by a registered public accounting firm or an associated person thereof.

(3) CENSURE OF BOARD MEMBERS; REMOVAL FROM OFFICE.—The Commission may, as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this Act or the securities laws, remove

from office or censure any member of the Board, if the Commission finds, on the record, after notice and opportunity for a hearing, that such member—

(A) has willfully violated any provision of this Act, the rules of the Board, or the securities laws;

(B) has willfully abused the authority of that member; or

(C) without reasonable justification or excuse, has failed to enforce compliance with any such provision or rule, or any professional standard by any registered public accounting firm or any associated person thereof.

15 USC 7218.

SEC. 108. ACCOUNTING STANDARDS.

(a) AMENDMENT TO SECURITIES ACT OF 1933.—Section 19 of the Securities Act of 1933 (15 U.S.C. 77s) is amended—

(1) by redesignating subsections (b) and (c) as subsections (c) and (d), respectively; and

(2) by inserting after subsection (a) the following:

"(b) RECOGNITION OF ACCOUNTING STANDARDS.—

"(1) IN GENERAL.—In carrying out its authority under subsection (a) and under section 13(b) of the Securities Exchange Act of 1934, the Commission may recognize, as 'generally accepted' for purposes of the securities laws, any accounting principles established by a standard setting body—

"(A) that—

"(i) is organized as a private entity;

"(ii) has, for administrative and operational purposes, a board of trustees (or equivalent body) serving in the public interest, the majority of whom are not, concurrent with their service on such board, and have not been during the 2-year period preceding such service, associated persons of any registered public accounting firm;

"(iii) is funded as provided in section 109 of the Sarbanes-Oxley Act of 2002;

"(iv) has adopted procedures to ensure prompt consideration, by majority vote of its members, of changes to accounting principles necessary to reflect emerging accounting issues and changing business practices; and

"(v) considers, in adopting accounting principles, the need to keep standards current in order to reflect changes in the business environment, the extent to which international convergence on high quality accounting standards is necessary or appropriate in the public interest and for the protection of investors; and

"(B) that the Commission determines has the capacity to assist the Commission in fulfilling the requirements of subsection (a) and section 13(b) of the Securities Exchange Act of 1934, because, at a minimum, the standard setting body is capable of improving the accuracy and effectiveness of financial reporting and the protection of investors under the securities laws.

"(2) ANNUAL REPORT.—A standard setting body described in paragraph (1) shall submit an annual report to the Commission and the public, containing audited financial statements of that standard setting body.".

(b) COMMISSION AUTHORITY.—The Commission shall promulgate such rules and regulations to carry out section 19(b) of the Securities Act of 1933, as added by this section, as it deems necessary or appropriate in the public interest or for the protection of investors. Regulations.

(c) NO EFFECT ON COMMISSION POWERS.—Nothing in this Act, including this section and the amendment made by this section, shall be construed to impair or limit the authority of the Commission to establish accounting principles or standards for purposes of enforcement of the securities laws.

(d) STUDY AND REPORT ON ADOPTING PRINCIPLES-BASED ACCOUNTING.—

(1) STUDY.—

(A) IN GENERAL.—The Commission shall conduct a study on the adoption by the United States financial reporting system of a principles-based accounting system.

(B) STUDY TOPICS.—The study required by subparagraph (A) shall include an examination of—

(i) the extent to which principles-based accounting and financial reporting exists in the United States;

(ii) the length of time required for change from a rules-based to a principles-based financial reporting system;

(iii) the feasibility of and proposed methods by which a principles-based system may be implemented; and

(iv) a thorough economic analysis of the implementation of a principles-based system.

(2) REPORT.—Not later than 1 year after the date of enactment of this Act, the Commission shall submit a report on the results of the study required by paragraph (1) to the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on Financial Services of the House of Representatives.

SEC. 109. FUNDING. 15 USC 7219.

(a) IN GENERAL.—The Board, and the standard setting body designated pursuant to section 19(b) of the Securities Act of 1933, as amended by section 108, shall be funded as provided in this section.

(b) ANNUAL BUDGETS.—The Board and the standard setting body referred to in subsection (a) shall each establish a budget for each fiscal year, which shall be reviewed and approved according to their respective internal procedures not less than 1 month prior to the commencement of the fiscal year to which the budget pertains (or at the beginning of the Board's first fiscal year, which may be a short fiscal year). The budget of the Board shall be subject to approval by the Commission. The budget for the first fiscal year of the Board shall be prepared and approved promptly following the appointment of the initial five Board members, to permit action by the Board of the organizational tasks contemplated by section 101(d).

(c) SOURCES AND USES OF FUNDS.—

(1) RECOVERABLE BUDGET EXPENSES.—The budget of the Board (reduced by any registration or annual fees received under section 102(e) for the year preceding the year for which the budget is being computed), and all of the budget of the standard setting body referred to in subsection (a), for each fiscal year of each of those 2 entities, shall be payable from annual accounting support fees, in accordance with subsections (d) and (e). Accounting support fees and other receipts of the Board and of such standard-setting body shall not be considered public monies of the United States.

(2) FUNDS GENERATED FROM THE COLLECTION OF MONETARY PENALTIES.—Subject to the availability in advance in an appropriations Act, and notwithstanding subsection (i), all funds collected by the Board as a result of the assessment of monetary penalties shall be used to fund a merit scholarship program for undergraduate and graduate students enrolled in accredited accounting degree programs, which program is to be administered by the Board or by an entity or agent identified by the Board.

(d) ANNUAL ACCOUNTING SUPPORT FEE FOR THE BOARD.—

(1) ESTABLISHMENT OF FEE.—The Board shall establish, with the approval of the Commission, a reasonable annual accounting support fee (or a formula for the computation thereof), as may be necessary or appropriate to establish and maintain the Board. Such fee may also cover costs incurred in the Board's first fiscal year (which may be a short fiscal year), or may be levied separately with respect to such short fiscal year.

(2) ASSESSMENTS.—The rules of the Board under paragraph (1) shall provide for the equitable allocation, assessment, and collection by the Board (or an agent appointed by the Board) of the fee established under paragraph (1), among issuers, in accordance with subsection (g), allowing for differentiation among classes of issuers, as appropriate.

(e) ANNUAL ACCOUNTING SUPPORT FEE FOR STANDARD SETTING BODY.—The annual accounting support fee for the standard setting body referred to in subsection (a)—

(1) shall be allocated in accordance with subsection (g), and assessed and collected against each issuer, on behalf of the standard setting body, by 1 or more appropriate designated collection agents, as may be necessary or appropriate to pay for the budget and provide for the expenses of that standard setting body, and to provide for an independent, stable source of funding for such body, subject to review by the Commission; and

(2) may differentiate among different classes of issuers.

(f) LIMITATION ON FEE.—The amount of fees collected under this section for a fiscal year on behalf of the Board or the standards setting body, as the case may be, shall not exceed the recoverable budget expenses of the Board or body, respectively (which may include operating, capital, and accrued items), referred to in subsection (c)(1).

(g) ALLOCATION OF ACCOUNTING SUPPORT FEES AMONG ISSUERS.—Any amount due from issuers (or a particular class of issuers) under this section to fund the budget of the Board or the standard setting body referred to in subsection (a) shall be allocated among and payable by each issuer (or each issuer in a particular class, as applicable) in an amount equal to the total of such amount, multiplied by a fraction—

(1) the numerator of which is the average monthly equity market capitalization of the issuer for the 12-month period immediately preceding the beginning of the fiscal year to which such budget relates; and

(2) the denominator of which is the average monthly equity market capitalization of all such issuers for such 12-month period.

(h) CONFORMING AMENDMENTS.—Section 13(b)(2) of the Securities Exchange Act of 1934 (15 U.S.C. 78m(b)(2)) is amended—

(1) in subparagraph (A), by striking "and" at the end; and

(2) in subparagraph (B), by striking the period at the end and inserting the following: "; and

"(C) notwithstanding any other provision of law, pay the allocable share of such issuer of a reasonable annual accounting support fee or fees, determined in accordance with section 109 of the Sarbanes-Oxley Act of 2002.".

(i) RULE OF CONSTRUCTION.—Nothing in this section shall be construed to render either the Board, the standard setting body referred to in subsection (a), or both, subject to procedures in Congress to authorize or appropriate public funds, or to prevent such organization from utilizing additional sources of revenue for its activities, such as earnings from publication sales, provided that each additional source of revenue shall not jeopardize, in the judgment of the Commission, the actual and perceived independence of such organization.

(j) START-UP EXPENSES OF THE BOARD.—From the unexpended balances of the appropriations to the Commission for fiscal year 2003, the Secretary of the Treasury is authorized to advance to the Board not to exceed the amount necessary to cover the expenses of the Board during its first fiscal year (which may be a short fiscal year).

TITLE II—AUDITOR INDEPENDENCE

SEC. 201. SERVICES OUTSIDE THE SCOPE OF PRACTICE OF AUDITORS.

(a) PROHIBITED ACTIVITIES.—Section 10A of the Securities Exchange Act of 1934 (15 U.S.C. 78j–1) is amended by adding at the end the following:

"(g) PROHIBITED ACTIVITIES.—Except as provided in subsection (h), it shall be unlawful for a registered public accounting firm (and any associated person of that firm, to the extent determined appropriate by the Commission) that performs for any issuer any audit required by this title or the rules of the Commission under this title or, beginning 180 days after the date of commencement of the operations of the Public Company Accounting Oversight Board established under section 101 of the Sarbanes-Oxley Act of 2002 (in this section referred to as the 'Board'), the rules of the Board, to provide to that issuer, contemporaneously with the audit, any non-audit service, including—

"(1) bookkeeping or other services related to the accounting records or financial statements of the audit client;

"(2) financial information systems design and implementation;

"(3) appraisal or valuation services, fairness opinions, or contribution-in-kind reports;
"(4) actuarial services;
"(5) internal audit outsourcing services;
"(6) management functions or human resources;
"(7) broker or dealer, investment adviser, or investment banking services;
"(8) legal services and expert services unrelated to the audit; and
"(9) any other service that the Board determines, by regulation, is impermissible.

"(h) PREAPPROVAL REQUIRED FOR NON-AUDIT SERVICES.—A registered public accounting firm may engage in any non-audit service, including tax services, that is not described in any of paragraphs (1) through (9) of subsection (g) for an audit client, only if the activity is approved in advance by the audit committee of the issuer, in accordance with subsection (i).".

15 USC 7231.

(b) EXEMPTION AUTHORITY.—The Board may, on a case by case basis, exempt any person, issuer, public accounting firm, or transaction from the prohibition on the provision of services under section 10A(g) of the Securities Exchange Act of 1934 (as added by this section), to the extent that such exemption is necessary or appropriate in the public interest and is consistent with the protection of investors, and subject to review by the Commission in the same manner as for rules of the Board under section 107.

SEC. 202. PREAPPROVAL REQUIREMENTS.

Section 10A of the Securities Exchange Act of 1934 (15 U.S.C. 78j–1), as amended by this Act, is amended by adding at the end the following:

"(i) PREAPPROVAL REQUIREMENTS.—
"(1) IN GENERAL.—
"(A) AUDIT COMMITTEE ACTION.—All auditing services (which may entail providing comfort letters in connection with securities underwritings or statutory audits required for insurance companies for purposes of State law) and non-audit services, other than as provided in subparagraph (B), provided to an issuer by the auditor of the issuer shall be preapproved by the audit committee of the issuer.
"(B) DE MINIMUS EXCEPTION.—The preapproval requirement under subparagraph (A) is waived with respect to the provision of non-audit services for an issuer, if—
"(i) the aggregate amount of all such non-audit services provided to the issuer constitutes not more than 5 percent of the total amount of revenues paid by the issuer to its auditor during the fiscal year in which the nonaudit services are provided;
"(ii) such services were not recognized by the issuer at the time of the engagement to be non-audit services; and
"(iii) such services are promptly brought to the attention of the audit committee of the issuer and approved prior to the completion of the audit by the audit committee or by 1 or more members of the audit committee who are members of the board of directors to whom authority to grant such approvals has been delegated by the audit committee.

"(2) DISCLOSURE TO INVESTORS.—Approval by an audit committee of an issuer under this subsection of a non-audit service to be performed by the auditor of the issuer shall be disclosed to investors in periodic reports required by section 13(a).
"(3) DELEGATION AUTHORITY.—The audit committee of an issuer may delegate to 1 or more designated members of the audit committee who are independent directors of the board of directors, the authority to grant preapprovals required by this subsection. The decisions of any member to whom authority is delegated under this paragraph to preapprove an activity under this subsection shall be presented to the full audit committee at each of its scheduled meetings.
"(4) APPROVAL OF AUDIT SERVICES FOR OTHER PURPOSES.—In carrying out its duties under subsection (m)(2), if the audit committee of an issuer approves an audit service within the scope of the engagement of the auditor, such audit service shall be deemed to have been preapproved for purposes of this subsection.".

SEC. 203. AUDIT PARTNER ROTATION.

Section 10A of the Securities Exchange Act of 1934 (15 U.S.C. 78j–1), as amended by this Act, is amended by adding at the end the following:

"(j) AUDIT PARTNER ROTATION.—It shall be unlawful for a registered public accounting firm to provide audit services to an issuer if the lead (or coordinating) audit partner (having primary responsibility for the audit), or the audit partner responsible for reviewing the audit, has performed audit services for that issuer in each of the 5 previous fiscal years of that issuer.".

SEC. 204. AUDITOR REPORTS TO AUDIT COMMITTEES.

Section 10A of the Securities Exchange Act of 1934 (15 U.S.C. 78j–1), as amended by this Act, is amended by adding at the end the following:

"(k) REPORTS TO AUDIT COMMITTEES.—Each registered public accounting firm that performs for any issuer any audit required by this title shall timely report to the audit committee of the issuer—
"(1) all critical accounting policies and practices to be used;
"(2) all alternative treatments of financial information within generally accepted accounting principles that have been discussed with management officials of the issuer, ramifications of the use of such alternative disclosures and treatments, and the treatment preferred by the registered public accounting firm; and
"(3) other material written communications between the registered public accounting firm and the management of the issuer, such as any management letter or schedule of unadjusted differences.".

SEC. 205. CONFORMING AMENDMENTS.

(a) DEFINITIONS.—Section 3(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)) is amended by adding at the end the following:

"(58) AUDIT COMMITTEE.—The term 'audit committee' means—
"(A) a committee (or equivalent body) established by and amongst the board of directors of an issuer for the

purpose of overseeing the accounting and financial reporting processes of the issuer and audits of the financial statements of the issuer; and

"(B) if no such committee exists with respect to an issuer, the entire board of directors of the issuer.

"(59) REGISTERED PUBLIC ACCOUNTING FIRM.—The term 'registered public accounting firm' has the same meaning as in section 2 of the Sarbanes-Oxley Act of 2002.".

(b) AUDITOR REQUIREMENTS.—Section 10A of the Securities Exchange Act of 1934 (15 U.S.C. 78j–1) is amended—

(1) by striking "an independent public accountant" each place that term appears and inserting "a registered public accounting firm";

(2) by striking "the independent public accountant" each place that term appears and inserting "the registered public accounting firm";

(3) in subsection (c), by striking "No independent public accountant" and inserting "No registered public accounting firm"; and

(4) in subsection (b)—

(A) by striking "the accountant" each place that term appears and inserting "the firm";

(B) by striking "such accountant" each place that term appears and inserting "such firm"; and

(C) in paragraph (4), by striking "the accountant's report" and inserting "the report of the firm".

(c) OTHER REFERENCES.—The Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) is amended—

(1) in section 12(b)(1) (15 U.S.C. 78l(b)(1)), by striking "independent public accountants" each place that term appears and inserting "a registered public accounting firm"; and

(2) in subsections (e) and (i) of section 17 (15 U.S.C. 78q), by striking "an independent public accountant" each place that term appears and inserting "a registered public accounting firm".

(d) CONFORMING AMENDMENT.—Section 10A(f) of the Securities Exchange Act of 1934 (15 U.S.C. 78k(f)) is amended— 15 USC 78j–1.

(1) by striking "DEFINITION" and inserting "DEFINITIONS"; and

(2) by adding at the end the following: "As used in this section, the term 'issuer' means an issuer (as defined in section 3), the securities of which are registered under section 12, or that is required to file reports pursuant to section 15(d), or that files or has filed 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.".

SEC. 206. CONFLICTS OF INTEREST.

Section 10A of the Securities Exchange Act of 1934 (15 U.S.C. 78j–1), as amended by this Act, is amended by adding at the end the following:

"(l) CONFLICTS OF INTEREST.—It shall be unlawful for a registered public accounting firm to perform for an issuer any audit service required by this title, if a chief executive officer, controller, chief financial officer, chief accounting officer, or any person serving in an equivalent position for the issuer, was employed by that registered independent public accounting firm and participated in any capacity in the audit of that issuer during the 1-year period preceding the date of the initiation of the audit.".

SEC. 207. STUDY OF MANDATORY ROTATION OF REGISTERED PUBLIC ACCOUNTING FIRMS. 15 USC 7232.

(a) STUDY AND REVIEW REQUIRED.—The Comptroller General of the United States shall conduct a study and review of the potential effects of requiring the mandatory rotation of registered public accounting firms.

(b) REPORT REQUIRED.—Not later than 1 year after the date of enactment of this Act, the Comptroller General shall submit a report to the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on Financial Services of the House of Representatives on the results of the study and review required by this section. Deadline.

(c) DEFINITION.—For purposes of this section, the term "mandatory rotation" refers to the imposition of a limit on the period of years in which a particular registered public accounting firm may be the auditor of record for a particular issuer.

SEC. 208. COMMISSION AUTHORITY. 15 USC 7233.

(a) COMMISSION REGULATIONS.—Not later than 180 days after the date of enactment of this Act, the Commission shall issue final regulations to carry out each of subsections (g) through (l) of section 10A of the Securities Exchange Act of 1934, as added by this title. Deadline.

(b) AUDITOR INDEPENDENCE.—It shall be unlawful for any registered public accounting firm (or an associated person thereof, as applicable) to prepare or issue any audit report with respect to any issuer, if the firm or associated person engages in any activity with respect to that issuer prohibited by any of subsections (g) through (l) of section 10A of the Securities Exchange Act of 1934, as added by this title, or any rule or regulation of the Commission or of the Board issued thereunder.

SEC. 209. CONSIDERATIONS BY APPROPRIATE STATE REGULATORY AUTHORITIES. 15 USC 7234.

In supervising nonregistered public accounting firms and their associated persons, appropriate State regulatory authorities should make an independent determination of the proper standards applicable, particularly taking into consideration the size and nature of the business of the accounting firms they supervise and the size and nature of the business of the clients of those firms. The standards applied by the Board under this Act should not be presumed to be applicable for purposes of this section for small and medium sized nonregistered public accounting firms.

TITLE III—CORPORATE RESPONSIBILITY

SEC. 301. PUBLIC COMPANY AUDIT COMMITTEES.

Section 10A of the Securities Exchange Act of 1934 (15 U.S.C. 78f) is amended by adding at the end the following: 15 USC 78j–1.

"(m) STANDARDS RELATING TO AUDIT COMMITTEES.—

"(1) COMMISSION RULES.—

Deadline.

"(A) IN GENERAL.—Effective not later than 270 days after the date of enactment of this subsection, the Commission shall, by rule, direct the national securities exchanges and national securities associations to prohibit the listing of any security of an issuer that is not in compliance with the requirements of any portion of paragraphs (2) through (6).

"(B) OPPORTUNITY TO CURE DEFECTS.—The rules of the Commission under subparagraph (A) shall provide for appropriate procedures for an issuer to have an opportunity to cure any defects that would be the basis for a prohibition under subparagraph (A), before the imposition of such prohibition.

"(2) RESPONSIBILITIES RELATING TO REGISTERED PUBLIC ACCOUNTING FIRMS.—The audit committee of each issuer, in its capacity as a committee of the board of directors, shall be directly responsible for the appointment, compensation, and oversight of the work of any registered public accounting firm employed by that issuer (including resolution of disagreements between management and the auditor regarding financial reporting) for the purpose of preparing or issuing an audit report or related work, and each such registered public accounting firm shall report directly to the audit committee.

"(3) INDEPENDENCE.—

"(A) IN GENERAL.—Each member of the audit committee of the issuer shall be a member of the board of directors of the issuer, and shall otherwise be independent.

"(B) CRITERIA.—In order to be considered to be independent for purposes of this paragraph, a member of an audit committee of an issuer may not, other than in his or her capacity as a member of the audit committee, the board of directors, or any other board committee—

"(i) accept any consulting, advisory, or other compensatory fee from the issuer; or

"(ii) be an affiliated person of the issuer or any subsidiary thereof.

"(C) EXEMPTION AUTHORITY.—The Commission may exempt from the requirements of subparagraph (B) a particular relationship with respect to audit committee members, as the Commission determines appropriate in light of the circumstances.

"(4) COMPLAINTS.—Each audit committee shall establish procedures for—

"(A) the receipt, retention, and treatment of complaints received by the issuer regarding accounting, internal accounting controls, or auditing matters; and

"(B) the confidential, anonymous submission by employees of the issuer of concerns regarding questionable accounting or auditing matters.

"(5) AUTHORITY TO ENGAGE ADVISERS.—Each audit committee shall have the authority to engage independent counsel and other advisers, as it determines necessary to carry out its duties.

"(6) FUNDING.—Each issuer shall provide for appropriate funding, as determined by the audit committee, in its capacity as a committee of the board of directors, for payment of compensation—

"(A) to the registered public accounting firm employed by the issuer for the purpose of rendering or issuing an audit report; and

"(B) to any advisers employed by the audit committee under paragraph (5).".

SEC. 302. CORPORATE RESPONSIBILITY FOR FINANCIAL REPORTS. 15 USC 7241.

(a) REGULATIONS REQUIRED.—The Commission shall, by rule, require, for each company filing periodic reports under section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m, 78o(d)), that the principal executive officer or officers and the principal financial officer or officers, or persons performing similar functions, certify in each annual or quarterly report filed or submitted under either such section of such Act that—

(1) the signing officer has reviewed the report;

(2) based on the officer's knowledge, the report does not contain any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which such statements were made, not misleading;

(3) based on such officer's knowledge, the financial statements, and other financial information included in the report, fairly present in all material respects the financial condition and results of operations of the issuer as of, and for, the periods presented in the report;

(4) the signing officers—

(A) are responsible for establishing and maintaining internal controls;

(B) have designed such internal controls to ensure that material information relating to the issuer and its consolidated subsidiaries is made known to such officers by others within those entities, particularly during the period in which the periodic reports are being prepared;

(C) have evaluated the effectiveness of the issuer's internal controls as of a date within 90 days prior to the report; and

(D) have presented in the report their conclusions about the effectiveness of their internal controls based on their evaluation as of that date;

(5) the signing officers have disclosed to the issuer's auditors and the audit committee of the board of directors (or persons fulfilling the equivalent function)—

(A) all significant deficiencies in the design or operation of internal controls which could adversely affect the issuer's ability to record, process, summarize, and report financial data and have identified for the issuer's auditors any material weaknesses in internal controls; and

(B) any fraud, whether or not material, that involves management or other employees who have a significant role in the issuer's internal controls; and

(6) the signing officers have indicated in the report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of their evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

(b) FOREIGN REINCORPORATIONS HAVE NO EFFECT.—Nothing in this section 302 shall be interpreted or applied in any way to allow any issuer to lessen the legal force of the statement required under this section 302, by an issuer having reincorporated or having engaged in any other transaction that resulted in the transfer of the corporate domicile or offices of the issuer from inside the United States to outside of the United States.

(c) DEADLINE.—The rules required by subsection (a) shall be effective not later than 30 days after the date of enactment of this Act.

15 USC 7242.

SEC. 303. IMPROPER INFLUENCE ON CONDUCT OF AUDITS.

(a) RULES TO PROHIBIT.—It shall be unlawful, in contravention of such rules or regulations as the Commission shall prescribe as necessary and appropriate in the public interest or for the protection of investors, for any officer or director of an issuer, or any other person acting under the direction thereof, to take any action to fraudulently influence, coerce, manipulate, or mislead any independent public or certified accountant engaged in the performance of an audit of the financial statements of that issuer for the purpose of rendering such financial statements materially misleading.

(b) ENFORCEMENT.—In any civil proceeding, the Commission shall have exclusive authority to enforce this section and any rule or regulation issued under this section.

(c) NO PREEMPTION OF OTHER LAW.—The provisions of subsection (a) shall be in addition to, and shall not supersede or preempt, any other provision of law or any rule or regulation issued thereunder.

(d) DEADLINE FOR RULEMAKING.—The Commission shall—

(1) propose the rules or regulations required by this section, not later than 90 days after the date of enactment of this Act; and

(2) issue final rules or regulations required by this section, not later than 270 days after that date of enactment.

15 USC 7243.

SEC. 304. FORFEITURE OF CERTAIN BONUSES AND PROFITS.

(a) ADDITIONAL COMPENSATION PRIOR TO NONCOMPLIANCE WITH COMMISSION FINANCIAL REPORTING REQUIREMENTS.—If an issuer is required to prepare an accounting restatement due to the material noncompliance of the issuer, as a result of misconduct, with any financial reporting requirement under the securities laws, the chief executive officer and chief financial officer of the issuer shall reimburse the issuer for—

(1) any bonus or other incentive-based or equity-based compensation received by that person from the issuer during the 12-month period following the first public issuance or filing with the Commission (whichever first occurs) of the financial document embodying such financial reporting requirement; and

(2) any profits realized from the sale of securities of the issuer during that 12-month period.

(b) COMMISSION EXEMPTION AUTHORITY.—The Commission may exempt any person from the application of subsection (a), as it deems necessary and appropriate.

SEC. 305. OFFICER AND DIRECTOR BARS AND PENALTIES.

(a) UNFITNESS STANDARD.—

(1) SECURITIES EXCHANGE ACT OF 1934.—Section 21(d)(2) of the Securities Exchange Act of 1934 (15 U.S.C. 78u(d)(2)) is amended by striking "substantial unfitness" and inserting "unfitness".

(2) SECURITIES ACT OF 1933.—Section 20(e) of the Securities Act of 1933 (15 U.S.C. 77t(e)) is amended by striking "substantial unfitness" and inserting "unfitness".

(b) EQUITABLE RELIEF.—Section 21(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78u(d)) is amended by adding at the end the following:

"(5) EQUITABLE RELIEF.—In any action or proceeding brought or instituted by the Commission under any provision of the securities laws, the Commission may seek, and any Federal court may grant, any equitable relief that may be appropriate or necessary for the benefit of investors.".

SEC. 306. INSIDER TRADES DURING PENSION FUND BLACKOUT PERIODS.

15 USC 7244.

(a) PROHIBITION OF INSIDER TRADING DURING PENSION FUND BLACKOUT PERIODS.—

(1) IN GENERAL.—Except to the extent otherwise provided by rule of the Commission pursuant to paragraph (3), it shall be unlawful for any director or executive officer of an issuer of any equity security (other than an exempted security), directly or indirectly, to purchase, sell, or otherwise acquire or transfer any equity security of the issuer (other than an exempted security) during any blackout period with respect to such equity security if such director or officer acquires such equity security in connection with his or her service or employment as a director or executive officer.

(2) REMEDY.—

(A) IN GENERAL.—Any profit realized by a director or executive officer referred to in paragraph (1) from any purchase, sale, or other acquisition or transfer in violation of this subsection shall inure to and be recoverable by the issuer, irrespective of any intention on the part of such director or executive officer in entering into the transaction.

(B) ACTIONS TO RECOVER PROFITS.—An action to recover profits in accordance with this subsection may be instituted at law or in equity in any court of competent jurisdiction by the issuer, or by the owner of any security of the issuer in the name and in behalf of the issuer if the issuer fails or refuses to bring such action within 60 days after the date of request, or fails diligently to prosecute the action thereafter, except that no such suit shall be brought more than 2 years after the date on which such profit was realized.

(3) RULEMAKING AUTHORIZED.—The Commission shall, in consultation with the Secretary of Labor, issue rules to clarify the application of this subsection and to prevent evasion thereof. Such rules shall provide for the application of the requirements of paragraph (1) with respect to entities treated as a single employer with respect to an issuer under section 414(b), (c), (m), or (o) of the Internal Revenue Code of 1986 to the extent necessary to clarify the application of such requirements and to prevent evasion thereof. Such rules may also provide for

appropriate exceptions from the requirements of this subsection, including exceptions for purchases pursuant to an automatic dividend reinvestment program or purchases or sales made pursuant to an advance election.

(4) BLACKOUT PERIOD.—For purposes of this subsection, the term "blackout period", with respect to the equity securities of any issuer—

(A) means any period of more than 3 consecutive business days during which the ability of not fewer than 50 percent of the participants or beneficiaries under all individual account plans maintained by the issuer to purchase, sell, or otherwise acquire or transfer an interest in any equity of such issuer held in such an individual account plan is temporarily suspended by the issuer or by a fiduciary of the plan; and

(B) does not include, under regulations which shall be prescribed by the Commission—

(i) a regularly scheduled period in which the participants and beneficiaries may not purchase, sell, or otherwise acquire or transfer an interest in any equity of such issuer, if such period is—

(I) incorporated into the individual account plan; and

(II) timely disclosed to employees before becoming participants under the individual account plan or as a subsequent amendment to the plan; or

(ii) any suspension described in subparagraph (A) that is imposed solely in connection with persons becoming participants or beneficiaries, or ceasing to be participants or beneficiaries, in an individual account plan by reason of a corporate merger, acquisition, divestiture, or similar transaction involving the plan or plan sponsor.

(5) INDIVIDUAL ACCOUNT PLAN.—For purposes of this subsection, the term "individual account plan" has the meaning provided in section 3(34) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1002(34), except that such term shall not include a one-participant retirement plan (within the meaning of section 101(i)(8)(B) of such Act (29 U.S.C. 1021(i)(8)(B))).

(6) NOTICE TO DIRECTORS, EXECUTIVE OFFICERS, AND THE COMMISSION.—In any case in which a director or executive officer is subject to the requirements of this subsection in connection with a blackout period (as defined in paragraph (4)) with respect to any equity securities, the issuer of such equity securities shall timely notify such director or officer and the Securities and Exchange Commission of such blackout period.

(b) NOTICE REQUIREMENTS TO PARTICIPANTS AND BENEFICIARIES UNDER ERISA.—

(1) IN GENERAL.—Section 101 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1021) is amended by redesignating the second subsection (h) as subsection (j), and by inserting after the first subsection (h) the following new subsection:

"(i) NOTICE OF BLACKOUT PERIODS TO PARTICIPANT OR BENEFICIARY UNDER INDIVIDUAL ACCOUNT PLAN.—

"(1) DUTIES OF PLAN ADMINISTRATOR.—In advance of the commencement of any blackout period with respect to an individual account plan, the plan administrator shall notify the plan participants and beneficiaries who are affected by such action in accordance with this subsection.

"(2) NOTICE REQUIREMENTS.—

"(A) IN GENERAL.—The notices described in paragraph (1) shall be written in a manner calculated to be understood by the average plan participant and shall include—

"(i) the reasons for the blackout period,

"(ii) an identification of the investments and other rights affected,

"(iii) the expected beginning date and length of the blackout period,

"(iv) in the case of investments affected, a statement that the participant or beneficiary should evaluate the appropriateness of their current investment decisions in light of their inability to direct or diversify assets credited to their accounts during the blackout period, and

"(v) such other matters as the Secretary may require by regulation.

"(B) NOTICE TO PARTICIPANTS AND BENEFICIARIES.—Except as otherwise provided in this subsection, notices described in paragraph (1) shall be furnished to all participants and beneficiaries under the plan to whom the blackout period applies at least 30 days in advance of the blackout period.

"(C) EXCEPTION TO 30-DAY NOTICE REQUIREMENT.—In any case in which—

"(i) a deferral of the blackout period would violate the requirements of subparagraph (A) or (B) of section 404(a)(1), and a fiduciary of the plan reasonably so determines in writing, or

"(ii) the inability to provide the 30-day advance notice is due to events that were unforeseeable or circumstances beyond the reasonable control of the plan administrator, and a fiduciary of the plan reasonably so determines in writing,

subparagraph (B) shall not apply, and the notice shall be furnished to all participants and beneficiaries under the plan to whom the blackout period applies as soon as reasonably possible under the circumstances unless such a notice in advance of the termination of the blackout period is impracticable.

"(D) WRITTEN NOTICE.—The notice required to be provided under this subsection shall be in writing, except that such notice may be in electronic or other form to the extent that such form is reasonably accessible to the recipient.

"(E) NOTICE TO ISSUERS OF EMPLOYER SECURITIES SUBJECT TO BLACKOUT PERIOD.—In the case of any blackout period in connection with an individual account plan, the plan administrator shall provide timely notice of such

blackout period to the issuer of any employer securities subject to such blackout period.

"(3) EXCEPTION FOR BLACKOUT PERIODS WITH LIMITED APPLICABILITY.—In any case in which the blackout period applies only to 1 or more participants or beneficiaries in connection with a merger, acquisition, divestiture, or similar transaction involving the plan or plan sponsor and occurs solely in connection with becoming or ceasing to be a participant or beneficiary under the plan by reason of such merger, acquisition, divestiture, or transaction, the requirement of this subsection that the notice be provided to all participants and beneficiaries shall be treated as met if the notice required under paragraph (1) is provided to such participants or beneficiaries to whom the blackout period applies as soon as reasonably practicable.

"(4) CHANGES IN LENGTH OF BLACKOUT PERIOD.—If, following the furnishing of the notice pursuant to this subsection, there is a change in the beginning date or length of the blackout period (specified in such notice pursuant to paragraph (2)(A)(iii)), the administrator shall provide affected participants and beneficiaries notice of the change as soon as reasonably practicable. In relation to the extended blackout period, such notice shall meet the requirements of paragraph (2)(D) and shall specify any material change in the matters referred to in clauses (i) through (v) of paragraph (2)(A).

"(5) REGULATORY EXCEPTIONS.—The Secretary may provide by regulation for additional exceptions to the requirements of this subsection which the Secretary determines are in the interests of participants and beneficiaries.

"(6) GUIDANCE AND MODEL NOTICES.—The Secretary shall issue guidance and model notices which meet the requirements of this subsection.

"(7) BLACKOUT PERIOD.—For purposes of this subsection—

"(A) IN GENERAL.—The term 'blackout period' means, in connection with an individual account plan, any period for which any ability of participants or beneficiaries under the plan, which is otherwise available under the terms of such plan, to direct or diversify assets credited to their accounts, to obtain loans from the plan, or to obtain distributions from the plan is temporarily suspended, limited, or restricted, if such suspension, limitation, or restriction is for any period of more than 3 consecutive business days.

"(B) EXCLUSIONS.—The term 'blackout period' does not include a suspension, limitation, or restriction—

"(i) which occurs by reason of the application of the securities laws (as defined in section 3(a)(47) of the Securities Exchange Act of 1934),

"(ii) which is a change to the plan which provides for a regularly scheduled suspension, limitation, or restriction which is disclosed to participants or beneficiaries through any summary of material modifications, any materials describing specific investment alternatives under the plan, or any changes thereto, or

"(iii) which applies only to 1 or more individuals, each of whom is the participant, an alternate payee (as defined in section 206(d)(3)(K)), or any other beneficiary pursuant to a qualified domestic relations order (as defined in section 206(d)(3)(B)(i)).

"(8) INDIVIDUAL ACCOUNT PLAN.—

"(A) IN GENERAL.—For purposes of this subsection, the term 'individual account plan' shall have the meaning provided such term in section 3(34), except that such term shall not include a one-participant retirement plan.

"(B) ONE-PARTICIPANT RETIREMENT PLAN.—For purposes of subparagraph (A), the term 'one-participant retirement plan' means a retirement plan that—

"(i) on the first day of the plan year—

"(I) covered only the employer (and the employer's spouse) and the employer owned the entire business (whether or not incorporated), or

"(II) covered only one or more partners (and their spouses) in a business partnership (including partners in an S or C corporation (as defined in section 1361(a) of the Internal Revenue Code of 1986)),

"(ii) meets the minimum coverage requirements of section 410(b) of the Internal Revenue Code of 1986 (as in effect on the date of the enactment of this paragraph) without being combined with any other plan of the business that covers the employees of the business,

"(iii) does not provide benefits to anyone except the employer (and the employer's spouse) or the partners (and their spouses),

"(iv) does not cover a business that is a member of an affiliated service group, a controlled group of corporations, or a group of businesses under common control, and

"(v) does not cover a business that leases employees.".

(2) ISSUANCE OF INITIAL GUIDANCE AND MODEL NOTICE.—The Secretary of Labor shall issue initial guidance and a model notice pursuant to section 101(i)(6) of the Employee Retirement Income Security Act of 1974 (as added by this subsection) not later than January 1, 2003. Not later than 75 days after the date of the enactment of this Act, the Secretary shall promulgate interim final rules necessary to carry out the amendments made by this subsection. Deadlines. Regulations.

(3) CIVIL PENALTIES FOR FAILURE TO PROVIDE NOTICE.—Section 502 of such Act (29 U.S.C. 1132) is amended—

(A) in subsection (a)(6), by striking "(5), or (6)" and inserting "(5), (6), or (7)";

(B) by redesignating paragraph (7) of subsection (c) as paragraph (8); and

(C) by inserting after paragraph (6) of subsection (c) the following new paragraph:

"(7) The Secretary may assess a civil penalty against a plan administrator of up to $100 a day from the date of the plan administrator's failure or refusal to provide notice to participants and beneficiaries in accordance with section 101(i). For purposes of this paragraph, each violation with respect to any single participant or beneficiary shall be treated as a separate violation.".

(3) PLAN AMENDMENTS.—If any amendment made by this subsection requires an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after the effective date of this section, if—

(A) during the period after such amendment made by this subsection takes effect and before such first plan year, the plan is operated in good faith compliance with the requirements of such amendment made by this subsection, and

(B) such plan amendment applies retroactively to the period after such amendment made by this subsection takes effect and before such first plan year.

(c) EFFECTIVE DATE.—The provisions of this section (including the amendments made thereby) shall take effect 180 days after the date of the enactment of this Act. Good faith compliance with the requirements of such provisions in advance of the issuance of applicable regulations thereunder shall be treated as compliance with such provisions.

15 USC 7245.

SEC. 307. RULES OF PROFESSIONAL RESPONSIBILITY FOR ATTORNEYS.

Deadline.

Not later than 180 days after the date of enactment of this Act, the Commission shall 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 in any way in the representation of issuers, including a rule—

(1) requiring an attorney to report evidence of a material violation of securities law or breach of fiduciary duty or similar violation by the company or any agent thereof, to the chief legal counsel or the chief executive officer of the company (or the equivalent thereof); and

(2) if the counsel or officer does not appropriately respond to the evidence (adopting, as necessary, appropriate remedial measures or sanctions with respect to the violation), requiring the attorney to 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.

15 USC 7246.

SEC. 308. FAIR FUNDS FOR INVESTORS.

(a) CIVIL PENALTIES ADDED TO DISGORGEMENT FUNDS FOR THE RELIEF OF VICTIMS.—If in any judicial or administrative action brought by the Commission under the securities laws (as such term is defined in section 3(a)(47) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(47)) the Commission obtains an order requiring disgorgement against any person for a violation of such laws or the rules or regulations thereunder, or such person agrees in settlement of any such action to such disgorgement, and the Commission also obtains pursuant to such laws a civil penalty against such person, the amount of such civil penalty shall, on the motion or at the direction of the Commission, be added to and become part of the disgorgement fund for the benefit of the victims of such violation.

(b) ACCEPTANCE OF ADDITIONAL DONATIONS.—The Commission is authorized to accept, hold, administer, and utilize gifts, bequests and devises of property, both real and personal, to the United States for a disgorgement fund described in subsection (a). Such gifts, bequests, and devises of money and proceeds from sales of other property received as gifts, bequests, or devises shall be deposited in the disgorgement fund and shall be available for allocation in accordance with subsection (a).

(c) STUDY REQUIRED.—

(1) SUBJECT OF STUDY.—The Commission shall review and analyze—

(A) enforcement actions by the Commission over the five years preceding the date of the enactment of this Act that have included proceedings to obtain civil penalties or disgorgements to identify areas where such proceedings may be utilized to efficiently, effectively, and fairly provide restitution for injured investors; and

(B) other methods to more efficiently, effectively, and fairly provide restitution to injured investors, including methods to improve the collection rates for civil penalties and disgorgements.

(2) REPORT REQUIRED.—The Commission shall report its findings to the Committee on Financial Services of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate within 180 days after of the date of the enactment of this Act, and shall use such findings to revise its rules and regulations as necessary. The report shall include a discussion of regulatory or legislative actions that are recommended or that may be necessary to address concerns identified in the study. Deadline.

(d) CONFORMING AMENDMENTS.—Each of the following provisions is amended by inserting ", except as otherwise provided in section 308 of the Sarbanes-Oxley Act of 2002" after "Treasury of the United States":

(1) Section 21(d)(3)(C)(i) of the Securities Exchange Act of 1934 (15 U.S.C. 78u(d)(3)(C)(i)).

(2) Section 21A(d)(1) of such Act (15 U.S.C. 78u-1(d)(1)).

(3) Section 20(d)(3)(A) of the Securities Act of 1933 (15 U.S.C. 77t(d)(3)(A)).

(4) Section 42(e)(3)(A) of the Investment Company Act of 1940 (15 U.S.C. 80a–41(e)(3)(A)).

(5) Section 209(e)(3)(A) of the Investment Advisers Act of 1940 (15 U.S.C. 80b–9(e)(3)(A)).

(e) DEFINITION.—As used in this section, the term "disgorgement fund" means a fund established in any administrative or judicial proceeding described in subsection (a).

TITLE IV—ENHANCED FINANCIAL DISCLOSURES

SEC. 401. DISCLOSURES IN PERIODIC REPORTS. 15 USC 7261.

(a) DISCLOSURES REQUIRED.—Section 13 of the Securities Exchange Act of 1934 (15 U.S.C. 78m) is amended by adding at the end the following:

"(i) ACCURACY OF FINANCIAL REPORTS.—Each financial report that contains financial statements, and that is required to be prepared in accordance with (or reconciled to) generally accepted accounting principles under this title and filed with the Commission shall reflect all material correcting adjustments that have been

identified by a registered public accounting firm in accordance with generally accepted accounting principles and the rules and regulations of the Commission.

Deadline. Regulations. "(j) OFF-BALANCE SHEET TRANSACTIONS.—Not later than 180 days after the date of enactment of the Sarbanes-Oxley Act of 2002, the Commission shall issue final rules providing that each annual and quarterly financial report required to be filed with the Commission shall disclose all material off-balance sheet transactions, arrangements, obligations (including contingent obligations), and other relationships of the issuer with unconsolidated entities or other persons, that may have a material current or future effect on financial condition, changes in financial condition, results of operations, liquidity, capital expenditures, capital resources, or significant components of revenues or expenses.".

Deadline. (b) COMMISSION RULES ON PRO FORMA FIGURES.—Not later than 180 days after the date of enactment of the Sarbanes-Oxley Act fo 2002, the Commission shall issue final rules providing that pro forma financial information included in any periodic or other report filed with the Commission pursuant to the securities laws, or in any public disclosure or press or other release, shall be presented in a manner that—

(1) does not contain an untrue statement of a material fact or omit to state a material fact necessary in order to make the pro forma financial information, in light of the circumstances under which it is presented, not misleading; and

(2) reconciles it with the financial condition and results of operations of the issuer under generally accepted accounting principles.

(c) STUDY AND REPORT ON SPECIAL PURPOSE ENTITIES.—

Deadline. (1) STUDY REQUIRED.—The Commission shall, not later than 1 year after the effective date of adoption of off-balance sheet disclosure rules required by section 13(j) of the Securities Exchange Act of 1934, as added by this section, complete a study of filings by issuers and their disclosures to determine—

(A) the extent of off-balance sheet transactions, including assets, liabilities, leases, losses, and the use of special purpose entities; and

(B) whether generally accepted accounting rules result in financial statements of issuers reflecting the economics of such off-balance sheet transactions to investors in a transparent fashion.

Deadline. (2) REPORT AND RECOMMENDATIONS.—Not later than 6 months after the date of completion of the study required by paragraph (1), the Commission shall submit a report to the President, the Committee on Banking, Housing, and Urban Affairs of the Senate, and the Committee on Financial Services of the House of Representatives, setting forth—

(A) the amount or an estimate of the amount of off-balance sheet transactions, including assets, liabilities, leases, and losses of, and the use of special purpose entities by, issuers filing periodic reports pursuant to section 13 or 15 of the Securities Exchange Act of 1934;

(B) the extent to which special purpose entities are used to facilitate off-balance sheet transactions;

(C) whether generally accepted accounting principles or the rules of the Commission result in financial statements of issuers reflecting the economics of such transactions to investors in a transparent fashion;

(D) whether generally accepted accounting principles specifically result in the consolidation of special purpose entities sponsored by an issuer in cases in which the issuer has the majority of the risks and rewards of the special purpose entity; and

(E) any recommendations of the Commission for improving the transparency and quality of reporting off-balance sheet transactions in the financial statements and disclosures required to be filed by an issuer with the Commission.

SEC. 402. ENHANCED CONFLICT OF INTEREST PROVISIONS.

(a) PROHIBITION ON PERSONAL LOANS TO EXECUTIVES.—Section 13 of the Securities Exchange Act of 1934 (15 U.S.C. 78m), as amended by this Act, is amended by adding at the end the following:

"(k) PROHIBITION ON PERSONAL LOANS TO EXECUTIVES.—

"(1) IN GENERAL.—It shall be unlawful for any issuer (as defined in section 2 of the Sarbanes-Oxley Act of 2002), directly or indirectly, including through any subsidiary, to extend or maintain credit, to arrange for the extension of credit, or to renew an extension of credit, in the form of a personal loan to or for any director or executive officer (or equivalent thereof) of that issuer. An extension of credit maintained by the issuer on the date of enactment of this subsection shall not be subject to the provisions of this subsection, provided that there is no material modification to any term of any such extension of credit or any renewal of any such extension of credit on or after that date of enactment.

"(2) LIMITATION.—Paragraph (1) does not preclude any home improvement and manufactured home loans (as that term is defined in section 5 of the Home Owners' Loan Act (12 U.S.C. 1464)), consumer credit (as defined in section 103 of the Truth in Lending Act (15 U.S.C. 1602)), or any extension of credit under an open end credit plan (as defined in section 103 of the Truth in Lending Act (15 U.S.C. 1602)), or a charge card (as defined in section 127(c)(4)(e) of the Truth in Lending Act (15 U.S.C. 1637(c)(4)(e)), or any extension of credit by a broker or dealer registered under section 15 of this title to an employee of that broker or dealer to buy, trade, or carry securities, that is permitted under rules or regulations of the Board of Governors of the Federal Reserve System pursuant to section 7 of this title (other than an extension of credit that would be used to purchase the stock of that issuer), that is—

"(A) made or provided in the ordinary course of the consumer credit business of such issuer;

"(B) of a type that is generally made available by such issuer to the public; and

"(C) made by such issuer on market terms, or terms that are no more favorable than those offered by the issuer to the general public for such extensions of credit.

"(3) RULE OF CONSTRUCTION FOR CERTAIN LOANS.—Paragraph (1) does not apply to any loan made or maintained

by an insured depository institution (as defined in section 3 of the Federal Deposit Insurance Act (12 U.S.C. 1813)), if the loan is subject to the insider lending restrictions of section 22(h) of the Federal Reserve Act (12 U.S.C. 375b).".

SEC. 403. DISCLOSURES OF TRANSACTIONS INVOLVING MANAGEMENT AND PRINCIPAL STOCKHOLDERS.

(a) AMENDMENT.—Section 16 of the Securities Exchange Act of 1934 (15 U.S.C. 78p) is amended by striking the heading of such section and subsection (a) and inserting the following:

"SEC. 16. DIRECTORS, OFFICERS, AND PRINCIPAL STOCKHOLDERS.

"(a) DISCLOSURES REQUIRED.—

"(1) DIRECTORS, OFFICERS, AND PRINCIPAL STOCKHOLDERS REQUIRED TO FILE.—Every person who is directly or indirectly the beneficial owner of more than 10 percent of any class of any equity security (other than an exempted security) which is registered pursuant to section 12, or who is a director or an officer of the issuer of such security, shall file the statements required by this subsection with the Commission (and, if such security is registered on a national securities exchange, also with the exchange).

"(2) TIME OF FILING.—The statements required by this subsection shall be filed—

"(A) at the time of the registration of such security on a national securities exchange or by the effective date of a registration statement filed pursuant to section 12(g);

"(B) within 10 days after he or she becomes such beneficial owner, director, or officer;

"(C) if there has been a change in such ownership, or if such person shall have purchased or sold a security-based swap agreement (as defined in section 206(b) of the Gramm-Leach-Bliley Act (15 U.S.C. 78c note)) involving such equity security, before the end of the second business day following the day on which the subject transaction has been executed, or at such other time as the Commission shall establish, by rule, in any case in which the Commission determines that such 2-day period is not feasible.

"(3) CONTENTS OF STATEMENTS.—A statement filed—

"(A) under subparagraph (A) or (B) of paragraph (2) shall contain a statement of the amount of all equity securities of such issuer of which the filing person is the beneficial owner; and

"(B) under subparagraph (C) of such paragraph shall indicate ownership by the filing person at the date of filing, any such changes in such ownership, and such purchases and sales of the security-based swap agreements as have occurred since the most recent such filing under such subparagraph.

Deadline. "(4) ELECTRONIC FILING AND AVAILABILITY.—Beginning not later than 1 year after the date of enactment of the Sarbanes-Oxley Act of 2002—

"(A) a statement filed under subparagraph (C) of paragraph (2) shall be filed electronically;

Deadline. "(B) the Commission shall provide each such statement on a publicly accessible Internet site not later than the end of the business day following that filing; and

"(C) the issuer (if the issuer maintains a corporate website) shall provide that statement on that corporate website, not later than the end of the business day following that filing.". Deadline.

(b) EFFECTIVE DATE.—The amendment made by this section shall be effective 30 days after the date of the enactment of this Act. 15 USC 78p note.

SEC. 404. MANAGEMENT ASSESSMENT OF INTERNAL CONTROLS. 15 USC 7262.

(a) RULES REQUIRED.—The Commission shall prescribe rules requiring each annual report required by section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)) to contain an internal control report, which shall—

(1) state the responsibility of management for establishing and maintaining an adequate internal control structure and procedures for financial reporting; and

(2) contain an assessment, as of the end of the most recent fiscal year of the issuer, of the effectiveness of the internal control structure and procedures of the issuer for financial reporting.

(b) INTERNAL CONTROL EVALUATION AND REPORTING.—With respect to the internal control assessment required by subsection (a), each registered public accounting firm that prepares or issues the audit report for the issuer shall attest to, and report on, the assessment made by the management of the issuer. An attestation made under this subsection shall be made in accordance with standards for attestation engagements issued or adopted by the Board. Any such attestation shall not be the subject of a separate engagement.

SEC. 405. EXEMPTION. 15 USC 7263.

Nothing in section 401, 402, or 404, the amendments made by those sections, or the rules of the Commission under those sections shall apply to any investment company registered under section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a–8).

SEC. 406. CODE OF ETHICS FOR SENIOR FINANCIAL OFFICERS. 15 USC 7264.

(a) CODE OF ETHICS DISCLOSURE.—The Commission shall issue rules to require each issuer, together with periodic reports required pursuant to section 13(a) or 15(d) of the Securities Exchange Act of 1934, to disclose whether or not, and if not, the reason therefor, such issuer has adopted a code of ethics for senior financial officers, applicable to its principal financial officer and comptroller or principal accounting officer, or persons performing similar functions. Regulations.

(b) CHANGES IN CODES OF ETHICS.—The Commission shall revise its regulations concerning matters requiring prompt disclosure on Form 8–K (or any successor thereto) to require the immediate disclosure, by means of the filing of such form, dissemination by the Internet or by other electronic means, by any issuer of any change in or waiver of the code of ethics for senior financial officers. Regulations.

(c) DEFINITION.—In this section, the term "code of ethics" means such standards as are reasonably necessary to promote—

(1) honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest between personal and professional relationships;

(2) full, fair, accurate, timely, and understandable disclosure in the periodic reports required to be filed by the issuer; and

(3) compliance with applicable governmental rules and regulations.

(d) DEADLINE FOR RULEMAKING.—The Commission shall—

(1) propose rules to implement this section, not later than 90 days after the date of enactment of this Act; and

(2) issue final rules to implement this section, not later than 180 days after that date of enactment.

15 USC 7265.

SEC. 407. DISCLOSURE OF AUDIT COMMITTEE FINANCIAL EXPERT.

(a) RULES DEFINING "FINANCIAL EXPERT".—The Commission shall issue rules, as necessary or appropriate in the public interest and consistent with the protection of investors, to require each issuer, together with periodic reports required pursuant to sections 13(a) and 15(d) of the Securities Exchange Act of 1934, to disclose whether or not, and if not, the reasons therefor, the audit committee of that issuer is comprised of at least 1 member who is a financial expert, as such term is defined by the Commission.

(b) CONSIDERATIONS.—In defining the term "financial expert" for purposes of subsection (a), the Commission shall consider whether a person has, through education and experience as a public accountant or auditor or a principal financial officer, comptroller, or principal accounting officer of an issuer, or from a position involving the performance of similar functions—

(1) an understanding of generally accepted accounting principles and financial statements;

(2) experience in—

(A) the preparation or auditing of financial statements of generally comparable issuers; and

(B) the application of such principles in connection with the accounting for estimates, accruals, and reserves;

(3) experience with internal accounting controls; and

(4) an understanding of audit committee functions.

(c) DEADLINE FOR RULEMAKING.—The Commission shall—

(1) propose rules to implement this section, not later than 90 days after the date of enactment of this Act; and

(2) issue final rules to implement this section, not later than 180 days after that date of enactment.

15 USC 7266.

SEC. 408. ENHANCED REVIEW OF PERIODIC DISCLOSURES BY ISSUERS.

(a) REGULAR AND SYSTEMATIC REVIEW.—The Commission shall review disclosures made by issuers reporting under section 13(a) of the Securities Exchange Act of 1934 (including reports filed on Form 10–K), and which have a class of securities listed on a national securities exchange or traded on an automated quotation facility of a national securities association, on a regular and systematic basis for the protection of investors. Such review shall include a review of an issuer's financial statement.

(b) REVIEW CRITERIA.—For purposes of scheduling the reviews required by subsection (a), the Commission shall consider, among other factors—

(1) issuers that have issued material restatements of financial results;

(2) issuers that experience significant volatility in their stock price as compared to other issuers;

(3) issuers with the largest market capitalization;

(4) emerging companies with disparities in price to earning ratios;

(5) issuers whose operations significantly affect any material sector of the economy; and

(6) any other factors that the Commission may consider relevant.

(c) MINIMUM REVIEW PERIOD.—In no event shall an issuer required to file reports under section 13(a) or 15(d) of the Securities Exchange Act of 1934 be reviewed under this section less frequently than once every 3 years.

SEC. 409. REAL TIME ISSUER DISCLOSURES.

Section 13 of the Securities Exchange Act of 1934 (15 U.S.C. 78m), as amended by this Act, is amended by adding at the end the following:

"(l) REAL TIME ISSUER DISCLOSURES.—Each issuer reporting under section 13(a) or 15(d) shall disclose to the public on a rapid and current basis such additional information concerning material changes in the financial condition or operations of the issuer, in plain English, which may include trend and qualitative information and graphic presentations, as the Commission determines, by rule, is necessary or useful for the protection of investors and in the public interest.".

TITLE V—ANALYST CONFLICTS OF INTEREST

SEC. 501. TREATMENT OF SECURITIES ANALYSTS BY REGISTERED SECURITIES ASSOCIATIONS AND NATIONAL SECURITIES EXCHANGES.

(a) RULES REGARDING SECURITIES ANALYSTS.—The Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) is amended by inserting after section 15C the following new section:

"SEC. 15D. SECURITIES ANALYSTS AND RESEARCH REPORTS.

15 USC 78*o*–6.

"(a) ANALYST PROTECTIONS.—The Commission, or upon the authorization and direction of the Commission, a registered securities association or national securities exchange, shall have adopted, not later than 1 year after the date of enactment of this section, rules reasonably designed to address conflicts of interest that can arise when securities analysts recommend equity securities in research reports and public appearances, in order to improve the objectivity of research and provide investors with more useful and reliable information, including rules designed—

Deadline.

"(1) to foster greater public confidence in securities research, and to protect the objectivity and independence of securities analysts, by—

"(A) restricting the prepublication clearance or approval of research reports by persons employed by the broker or dealer who are engaged in investment banking activities, or persons not directly responsible for investment research, other than legal or compliance staff;

"(B) limiting the supervision and compensatory evaluation of securities analysts to officials employed by the broker or dealer who are not engaged in investment banking activities; and

"(C) requiring that a broker or dealer and persons employed by a broker or dealer who are involved with investment banking activities may not, directly or indirectly, retaliate against or threaten to retaliate against any securities analyst employed by that broker or dealer or its affiliates as a result of an adverse, negative, or otherwise unfavorable research report that may adversely affect the present or prospective investment banking relationship of the broker or dealer with the issuer that is the subject of the research report, except that such rules may not limit the authority of a broker or dealer to discipline a securities analyst for causes other than such research report in accordance with the policies and procedures of the firm;

"(2) to define periods during which brokers or dealers who have participated, or are to participate, in a public offering of securities as underwriters or dealers should not publish or otherwise distribute research reports relating to such securities or to the issuer of such securities;

"(3) to establish structural and institutional safeguards within registered brokers or dealers to assure that securities analysts are separated by appropriate informational partitions within the firm from the review, pressure, or oversight of those whose involvement in investment banking activities might potentially bias their judgment or supervision; and

"(4) to address such other issues as the Commission, or such association or exchange, determines appropriate.

"(b) DISCLOSURE.—The Commission, or upon the authorization and direction of the Commission, a registered securities association or national securities exchange, shall have adopted, not later than 1 year after the date of enactment of this section, rules reasonably designed to require each securities analyst to disclose in public appearances, and each registered broker or dealer to disclose in each research report, as applicable, conflicts of interest that are known or should have been known by the securities analyst or the broker or dealer, to exist at the time of the appearance or the date of distribution of the report, including—

"(1) the extent to which the securities analyst has debt or equity investments in the issuer that is the subject of the appearance or research report;

"(2) whether any compensation has been received by the registered broker or dealer, or any affiliate thereof, including the securities analyst, from the issuer that is the subject of the appearance or research report, subject to such exemptions as the Commission may determine appropriate and necessary to prevent disclosure by virtue of this paragraph of material non-public information regarding specific potential future investment banking transactions of such issuer, as is appropriate in the public interest and consistent with the protection of investors;

"(3) whether an issuer, the securities of which are recommended in the appearance or research report, currently is, or during the 1-year period preceding the date of the appearance or date of distribution of the report has been, a client of the registered broker or dealer, and if so, stating the types of services provided to the issuer;

"(4) whether the securities analyst received compensation with respect to a research report, based upon (among any other factors) the investment banking revenues (either generally or specifically earned from the issuer being analyzed) of the registered broker or dealer; and

"(5) such other disclosures of conflicts of interest that are material to investors, research analysts, or the broker or dealer as the Commission, or such association or exchange, determines appropriate.

"(c) DEFINITIONS.—In this section—

"(1) the term 'securities analyst' means any associated person of a registered broker or dealer that is principally responsible for, and any associated person who reports directly or indirectly to a securities analyst in connection with, the preparation of the substance of a research report, whether or not any such person has the job title of 'securities analyst'; and

"(2) the term 'research report' means a written or electronic communication that includes an analysis of equity securities of individual companies or industries, and that provides information reasonably sufficient upon which to base an investment decision.".

(b) ENFORCEMENT.—Section 21B(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78u–2(a)) is amended by inserting "15D," before "15B".

(c) COMMISSION AUTHORITY.—The Commission may promulgate and amend its regulations, or direct a registered securities association or national securities exchange to promulgate and amend its rules, to carry out section 15D of the Securities Exchange Act of 1934, as added by this section, as is necessary for the protection of investors and in the public interest. 15 USC 78*o*–6 note.

TITLE VI—COMMISSION RESOURCES AND AUTHORITY

SEC. 601. AUTHORIZATION OF APPROPRIATIONS.

Section 35 of the Securities Exchange Act of 1934 (15 U.S.C. 78kk) is amended to read as follows:

"SEC. 35. AUTHORIZATION OF APPROPRIATIONS.

"In addition to any other funds authorized to be appropriated to the Commission, there are authorized to be appropriated to carry out the functions, powers, and duties of the Commission, $776,000,000 for fiscal year 2003, of which—

"(1) $102,700,000 shall be available to fund additional compensation, including salaries and benefits, as authorized in the Investor and Capital Markets Fee Relief Act (Public Law 107–123; 115 Stat. 2390 et seq.);

"(2) $108,400,000 shall be available for information technology, security enhancements, and recovery and mitigation activities in light of the terrorist attacks of September 11, 2001; and

"(3) $98,000,000 shall be available to add not fewer than an additional 200 qualified professionals to provide enhanced oversight of auditors and audit services required by the Federal securities laws, and to improve Commission investigative and

disciplinary efforts with respect to such auditors and services, as well as for additional professional support staff necessary to strengthen the programs of the Commission involving Full Disclosure and Prevention and Suppression of Fraud, risk management, industry technology review, compliance, inspections, examinations, market regulation, and investment management.".

SEC. 602. APPEARANCE AND PRACTICE BEFORE THE COMMISSION.

The Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) is amended by inserting after section 4B the following:

15 USC 78d–3.

"SEC. 4C. APPEARANCE AND PRACTICE BEFORE THE COMMISSION.

"(a) AUTHORITY TO CENSURE.—The Commission may censure any person, or deny, temporarily or permanently, to any person the privilege of appearing or practicing before the Commission in any way, if that person is found by the Commission, after notice and opportunity for hearing in the matter—

"(1) not to possess the requisite qualifications to represent others;

"(2) to be lacking in character or integrity, or to have engaged in unethical or improper professional conduct; or

"(3) to have willfully violated, or willfully aided and abetted the violation of, any provision of the securities laws or the rules and regulations issued thereunder.

"(b) DEFINITION.—With respect to any registered public accounting firm or associated person, for purposes of this section, the term 'improper professional conduct' means—

"(1) intentional or knowing conduct, including reckless conduct, that results in a violation of applicable professional standards; and

"(2) negligent conduct in the form of—

"(A) a single instance of highly unreasonable conduct that results in a violation of applicable professional standards in circumstances in which the registered public accounting firm or associated person knows, or should know, that heightened scrutiny is warranted; or

"(B) repeated instances of unreasonable conduct, each resulting in a violation of applicable professional standards, that indicate a lack of competence to practice before the Commission.".

SEC. 603. FEDERAL COURT AUTHORITY TO IMPOSE PENNY STOCK BARS.

(a) SECURITIES EXCHANGE ACT OF 1934.—Section 21(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78u(d)), as amended by this Act, is amended by adding at the end the following:

"(6) AUTHORITY OF A COURT TO PROHIBIT PERSONS FROM PARTICIPATING IN AN OFFERING OF PENNY STOCK.—

"(A) IN GENERAL.—In any proceeding under paragraph (1) against any person participating in, or, at the time of the alleged misconduct who was participating in, an offering of penny stock, the court may prohibit that person from participating in an offering of penny stock, conditionally or unconditionally, and permanently or for such period of time as the court shall determine.

"(B) DEFINITION.—For purposes of this paragraph, the term 'person participating in an offering of penny stock' includes any person engaging in activities with a broker, dealer, or issuer for purposes of issuing, trading, or inducing or attempting to induce the purchase or sale of, any penny stock. The Commission may, by rule or regulation, define such term to include other activities, and may, by rule, regulation, or order, exempt any person or class of persons, in whole or in part, conditionally or unconditionally, from inclusion in such term.".

(b) SECURITIES ACT OF 1933.—Section 20 of the Securities Act of 1933 (15 U.S.C. 77t) is amended by adding at the end the following:

"(g) AUTHORITY OF A COURT TO PROHIBIT PERSONS FROM PARTICIPATING IN AN OFFERING OF PENNY STOCK.—

"(1) IN GENERAL.—In any proceeding under subsection (a) against any person participating in, or, at the time of the alleged misconduct, who was participating in, an offering of penny stock, the court may prohibit that person from participating in an offering of penny stock, conditionally or unconditionally, and permanently or for such period of time as the court shall determine.

"(2) DEFINITION.—For purposes of this subsection, the term 'person participating in an offering of penny stock' includes any person engaging in activities with a broker, dealer, or issuer for purposes of issuing, trading, or inducing or attempting to induce the purchase or sale of, any penny stock. The Commission may, by rule or regulation, define such term to include other activities, and may, by rule, regulation, or order, exempt any person or class of persons, in whole or in part, conditionally or unconditionally, from inclusion in such term.".

SEC. 604. QUALIFICATIONS OF ASSOCIATED PERSONS OF BROKERS AND DEALERS.

(a) BROKERS AND DEALERS.—Section 15(b)(4) of the Securities Exchange Act of 1934 (15 U.S.C. 78o) is amended—

(1) by striking subparagraph (F) and inserting the following:

"(F) is subject to any order of the Commission barring or suspending the right of the person to be associated with a broker or dealer;"; and

(2) in subparagraph (G), by striking the period at the end and inserting the following: "; or

"(H) is subject to any final order of a State securities commission (or any agency or officer performing like functions), State authority that supervises or examines banks, savings associations, or credit unions, State insurance commission (or any agency or office performing like functions), an appropriate Federal banking agency (as defined in section 3 of the Federal Deposit Insurance Act (12 U.S.C. 1813(q))), or the National Credit Union Administration, that—

"(i) bars such person from association with an entity regulated by such commission, authority, agency, or officer, or from engaging in the business of securities, insurance, banking, savings association activities, or credit union activities; or

"(ii) constitutes a final order based on violations of any laws or regulations that prohibit fraudulent, manipulative, or deceptive conduct.".

(b) INVESTMENT ADVISERS.—Section 203(e) of the Investment Advisers Act of 1940 (15 U.S.C. 80b–3(e)) is amended—

(1) by striking paragraph (7) and inserting the following:

"(7) is subject to any order of the Commission barring or suspending the right of the person to be associated with an investment adviser;";

(2) in paragraph (8), by striking the period at the end and inserting "; or"; and

(3) by adding at the end the following:

"(9) is subject to any final order of a State securities commission (or any agency or officer performing like functions), State authority that supervises or examines banks, savings associations, or credit unions, State insurance commission (or any agency or office performing like functions), an appropriate Federal banking agency (as defined in section 3 of the Federal Deposit Insurance Act (12 U.S.C. 1813(q))), or the National Credit Union Administration, that—

"(A) bars such person from association with an entity regulated by such commission, authority, agency, or officer, or from engaging in the business of securities, insurance, banking, savings association activities, or credit union activities; or

"(B) constitutes a final order based on violations of any laws or regulations that prohibit fraudulent, manipulative, or deceptive conduct.".

(c) CONFORMING AMENDMENTS.—

(1) SECURITIES EXCHANGE ACT OF 1934.—The Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) is amended—

(A) in section 3(a)(39)(F) (15 U.S.C. 78c(a)(39)(F))—

(i) by striking "or (G)" and inserting "(H), or (G)"; and

(ii) by inserting ", or is subject to an order or finding," before "enumerated";

(B) in each of section 15(b)(6)(A)(i) (15 U.S.C. 78o(b)(6)(A)(i)), paragraphs (2) and (4) of section 15B(c) (15 U.S.C. 78o–4(c)), and subparagraphs (A) and (C) of section 15C(c)(1) (15 U.S.C. 78o–5(c)(1))—

(i) by striking "or (G)" each place that term appears and inserting "(H), or (G)"; and

(ii) by striking "or omission" each place that term appears, and inserting ", or is subject to an order or finding,"; and

(C) in each of paragraphs (3)(A) and (4)(C) of section 17A(c) (15 U.S.C. 78q–1(c))—

(i) by striking "or (G)" each place that term appears and inserting "(H), or (G)"; and

(ii) by inserting ", or is subject to an order or finding," before "enumerated" each place that term appears.

(2) INVESTMENT ADVISERS ACT OF 1940.—Section 203(f) of the Investment Advisers Act of 1940 (15 U.S.C. 80b–3(f)) is amended—

(A) by striking "or (8)" and inserting "(8), or (9)"; and

(B) by inserting "or (3)" after "paragraph (2)".

TITLE VII—STUDIES AND REPORTS

SEC. 701. GAO STUDY AND REPORT REGARDING CONSOLIDATION OF PUBLIC ACCOUNTING FIRMS. 15 USC 7201 note.

(a) STUDY REQUIRED.—The Comptroller General of the United States shall conduct a study—

(1) to identify—

(A) the factors that have led to the consolidation of public accounting firms since 1989 and the consequent reduction in the number of firms capable of providing audit services to large national and multi-national business organizations that are subject to the securities laws;

(B) the present and future impact of the condition described in subparagraph (A) on capital formation and securities markets, both domestic and international; and

(C) solutions to any problems identified under subparagraph (B), including ways to increase competition and the number of firms capable of providing audit services to large national and multinational business organizations that are subject to the securities laws;

(2) of the problems, if any, faced by business organizations that have resulted from limited competition among public accounting firms, including—

(A) higher costs;

(B) lower quality of services;

(C) impairment of auditor independence; or

(D) lack of choice; and

(3) whether and to what extent Federal or State regulations impede competition among public accounting firms.

(b) CONSULTATION.—In planning and conducting the study under this section, the Comptroller General shall consult with—

(1) the Commission;

(2) the regulatory agencies that perform functions similar to the Commission within the other member countries of the Group of Seven Industrialized Nations;

(3) the Department of Justice; and

(4) any other public or private sector organization that the Comptroller General considers appropriate.

(c) REPORT REQUIRED.—Not later than 1 year after the date of enactment of this Act, the Comptroller General shall submit a report on the results of the study required by this section to the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on Financial Services of the House of Representatives. Deadline.

SEC. 702. COMMISSION STUDY AND REPORT REGARDING CREDIT RATING AGENCIES.

(a) STUDY REQUIRED.—

(1) IN GENERAL.—The Commission shall conduct a study of the role and function of credit rating agencies in the operation of the securities market.

(2) AREAS OF CONSIDERATION.—The study required by this subsection shall examine—

(A) the role of credit rating agencies in the evaluation of issuers of securities;

(B) the importance of that role to investors and the functioning of the securities markets;

(C) any impediments to the accurate appraisal by credit rating agencies of the financial resources and risks of issuers of securities;

(D) any barriers to entry into the business of acting as a credit rating agency, and any measures needed to remove such barriers;

(E) any measures which may be required to improve the dissemination of information concerning such resources and risks when credit rating agencies announce credit ratings; and

(F) any conflicts of interest in the operation of credit rating agencies and measures to prevent such conflicts or ameliorate the consequences of such conflicts.

Deadline. (b) REPORT REQUIRED.—The Commission shall submit a report on the study required by subsection (a) to the President, the Committee on Financial Services of the House of Representatives, and the Committee on Banking, Housing, and Urban Affairs of the Senate not later than 180 days after the date of enactment of this Act.

SEC. 703. STUDY AND REPORT ON VIOLATORS AND VIOLATIONS.

(a) STUDY.—The Commission shall conduct a study to determine, based upon information for the period from January 1, 1998, to December 31, 2001—

(1) the number of securities professionals, defined as public accountants, public accounting firms, investment bankers, investment advisers, brokers, dealers, attorneys, and other securities professionals practicing before the Commission—

(A) who have been found to have aided and abetted a violation of the Federal securities laws, including rules or regulations promulgated thereunder (collectively referred to in this section as "Federal securities laws"), but who have not been sanctioned, disciplined, or otherwise penalized as a primary violator in any administrative action or civil proceeding, including in any settlement of such an action or proceeding (referred to in this section as "aiders and abettors"); and

(B) who have been found to have been primary violators of the Federal securities laws;

(2) a description of the Federal securities laws violations committed by aiders and abettors and by primary violators, including—

(A) the specific provision of the Federal securities laws violated;

(B) the specific sanctions and penalties imposed upon such aiders and abettors and primary violators, including the amount of any monetary penalties assessed upon and collected from such persons;

(C) the occurrence of multiple violations by the same person or persons, either as an aider or abettor or as a primary violator; and

(D) whether, as to each such violator, disciplinary sanctions have been imposed, including any censure, suspension, temporary bar, or permanent bar to practice before the Commission; and

(3) the amount of disgorgement, restitution, or any other fines or payments that the Commission has assessed upon and collected from, aiders and abettors and from primary violators.

(b) REPORT.—A report based upon the study conducted pursuant to subsection (a) shall be submitted to the Committee on Banking, Housing, and Urban Affairs of the Senate, and the Committee on Financial Services of the House of Representatives not later than 6 months after the date of enactment of this Act.

SEC. 704. STUDY OF ENFORCEMENT ACTIONS.

(a) STUDY REQUIRED.—The Commission shall review and analyze all enforcement actions by the Commission involving violations of reporting requirements imposed under the securities laws, and restatements of financial statements, over the 5-year period preceding the date of enactment of this Act, to identify areas of reporting that are most susceptible to fraud, inappropriate manipulation, or inappropriate earnings management, such as revenue recognition and the accounting treatment of off-balance sheet special purpose entities.

(b) REPORT REQUIRED.—The Commission shall report its findings to the Committee on Financial Services of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate, not later than 180 days after the date of enactment of this Act, and shall use such findings to revise its rules and regulations, as necessary. The report shall include a discussion of regulatory or legislative steps that are recommended or that may be necessary to address concerns identified in the study. Deadline.

SEC. 705. STUDY OF INVESTMENT BANKS.

(a) GAO STUDY.—The Comptroller General of the United States shall conduct a study on whether investment banks and financial advisers assisted public companies in manipulating their earnings and obfuscating their true financial condition. The study should address the rule of investment banks and financial advisers—

(1) in the collapse of the Enron Corporation, including with respect to the design and implementation of derivatives transactions, transactions involving special purpose vehicles, and other financial arrangements that may have had the effect of altering the company's reported financial statements in ways that obscured the true financial picture of the company;

(2) in the failure of Global Crossing, including with respect to transactions involving swaps of fiberoptic cable capacity, in the designing transactions that may have had the effect of altering the company's reported financial statements in ways that obscured the true financial picture of the company; and

(3) generally, in creating and marketing transactions which may have been designed solely to enable companies to manipulate revenue streams, obtain loans, or move liabilities off balance sheets without altering the economic and business risks faced by the companies or any other mechanism to obscure a company's financial picture.

(b) REPORT.—The Comptroller General shall report to Congress not later than 180 days after the date of enactment of this Act on the results of the study required by this section. The report shall include a discussion of regulatory or legislative steps that Deadline.

are recommended or that may be necessary to address concerns identified in the study.

Corporate and Criminal Fraud Accountability Act of 2002.

TITLE VIII—CORPORATE AND CRIMINAL FRAUD ACCOUNTABILITY

18 USC 1501 note.

SEC. 801. SHORT TITLE.

This title may be cited as the "Corporate and Criminal Fraud Accountability Act of 2002".

SEC. 802. CRIMINAL PENALTIES FOR ALTERING DOCUMENTS.

(a) IN GENERAL.—Chapter 73 of title 18, United States Code, is amended by adding at the end the following:

"§ 1519. Destruction, alteration, or falsification of records in Federal investigations and bankruptcy

"Whoever knowingly alters, destroys, mutilates, conceals, covers up, falsifies, or makes a false entry in any record, document, or tangible object with the intent to impede, obstruct, or influence the investigation or proper administration of any matter within the jurisdiction of any department or agency of the United States or any case filed under title 11, or in relation to or contemplation of any such matter or case, shall be fined under this title, imprisoned not more than 20 years, or both.

"§ 1520. Destruction of corporate audit records

"(a)(1) Any accountant who conducts an audit of an issuer of securities to which section 10A(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78j–1(a)) applies, shall maintain all audit or review workpapers for a period of 5 years from the end of the fiscal period in which the audit or review was concluded.

Regulations.

"(2) The Securities and Exchange Commission shall promulgate, within 180 days, after adequate notice and an opportunity for comment, such rules and regulations, as are reasonably necessary, relating to the retention of relevant records such as workpapers, documents that form the basis of an audit or review, memoranda, correspondence, communications, other documents, and records (including electronic records) which are created, sent, or received in connection with an audit or review and contain conclusions, opinions, analyses, or financial data relating to such an audit or review, which is conducted by any accountant who conducts an audit of an issuer of securities to which section 10A(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78j–1(a)) applies. The Commission may, from time to time, amend or supplement the rules and regulations that it is required to promulgate under this section, after adequate notice and an opportunity for comment, in order to ensure that such rules and regulations adequately comport with the purposes of this section.

"(b) Whoever knowingly and willfully violates subsection (a)(1), or any rule or regulation promulgated by the Securities and Exchange Commission under subsection (a)(2), shall be fined under this title, imprisoned not more than 10 years, or both.

"(c) Nothing in this section shall be deemed to diminish or relieve any person of any other duty or obligation imposed by Federal or State law or regulation to maintain, or refrain from destroying, any document.".

(b) CLERICAL AMENDMENT.—The table of sections at the beginning of chapter 73 of title 18, United States Code, is amended by adding at the end the following new items:

"1519. Destruction, alteration, or falsification of records in Federal investigations and bankruptcy.

"1520. Destruction of corporate audit records.".

SEC. 803. DEBTS NONDISCHARGEABLE IF INCURRED IN VIOLATION OF SECURITIES FRAUD LAWS.

Section 523(a) of title 11, United States Code, is amended—

(1) in paragraph (17), by striking "or" after the semicolon;

(2) in paragraph (18), by striking the period at the end and inserting "; or"; and

(3) by adding at the end, the following:

"(19) that—

"(A) is for—

"(i) the violation of any of the Federal securities laws (as that term is defined in section 3(a)(47) of the Securities Exchange Act of 1934), any of the State securities laws, or any regulation or order issued under such Federal or State securities laws; or

"(ii) common law fraud, deceit, or manipulation in connection with the purchase or sale of any security; and

"(B) results from—

"(i) any judgment, order, consent order, or decree entered in any Federal or State judicial or administrative proceeding;

"(ii) any settlement agreement entered into by the debtor; or

"(iii) any court or administrative order for any damages, fine, penalty, citation, restitutionary payment, disgorgement payment, attorney fee, cost, or other payment owed by the debtor.".

SEC. 804. STATUTE OF LIMITATIONS FOR SECURITIES FRAUD.

(a) IN GENERAL.—Section 1658 of title 28, United States Code, is amended—

(1) by inserting "(a)" before "Except"; and

(2) by adding at the end the following:

"(b) Notwithstanding subsection (a), a private right of action that involves a claim of fraud, deceit, manipulation, or contrivance in contravention of a regulatory requirement concerning the securities laws, as defined in section 3(a)(47) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(47)), may be brought not later than the earlier of—

"(1) 2 years after the discovery of the facts constituting the violation; or

"(2) 5 years after such violation.".

28 USC 1658 note.

(b) EFFECTIVE DATE.—The limitations period provided by section 1658(b) of title 28, United States Code, as added by this section, shall apply to all proceedings addressed by this section that are commenced on or after the date of enactment of this Act.

28 USC 1658 note.

(c) NO CREATION OF ACTIONS.—Nothing in this section shall create a new, private right of action.

28 USC 994 note.

SEC. 805. REVIEW OF FEDERAL SENTENCING GUIDELINES FOR OBSTRUCTION OF JUSTICE AND EXTENSIVE CRIMINAL FRAUD.

(a) ENHANCEMENT OF FRAUD AND OBSTRUCTION OF JUSTICE SENTENCES.—Pursuant to section 994 of title 28, United States Code, and in accordance with this section, the United States Sentencing Commission shall review and amend, as appropriate, the Federal Sentencing Guidelines and related policy statements to ensure that—

(1) the base offense level and existing enhancements contained in United States Sentencing Guideline 2J1.2 relating to obstruction of justice are sufficient to deter and punish that activity;

(2) the enhancements and specific offense characteristics relating to obstruction of justice are adequate in cases where—

(A) the destruction, alteration, or fabrication of evidence involves—

(i) a large amount of evidence, a large number of participants, or is otherwise extensive;

(ii) the selection of evidence that is particularly probative or essential to the investigation; or

(iii) more than minimal planning; or

(B) the offense involved abuse of a special skill or a position of trust;

(3) the guideline offense levels and enhancements for violations of section 1519 or 1520 of title 18, United States Code, as added by this title, are sufficient to deter and punish that activity;

(4) a specific offense characteristic enhancing sentencing is provided under United States Sentencing Guideline 2B1.1 (as in effect on the date of enactment of this Act) for a fraud offense that endangers the solvency or financial security of a substantial number of victims; and

(5) the guidelines that apply to organizations in United States Sentencing Guidelines, chapter 8, are sufficient to deter and punish organizational criminal misconduct.

Deadline.

(b) EMERGENCY AUTHORITY AND DEADLINE FOR COMMISSION ACTION.—The United States Sentencing Commission is requested to promulgate the guidelines or amendments provided for under this section as soon as practicable, and in any event not later than 180 days after the date of enactment of this Act, in accordance with the procedures set forth in section 219(a) of the Sentencing Reform Act of 1987, as though the authority under that Act had not expired.

SEC. 806. PROTECTION FOR EMPLOYEES OF PUBLICLY TRADED COMPANIES WHO PROVIDE EVIDENCE OF FRAUD.

(a) IN GENERAL.—Chapter 73 of title 18, United States Code, is amended by inserting after section 1514 the following:

"§ 1514A. Civil action to protect against retaliation in fraud cases

"(a) WHISTLEBLOWER PROTECTION FOR EMPLOYEES OF PUBLICLY TRADED COMPANIES.—No company with a class of securities registered under section 12 of the Securities Exchange Act of 1934 (15 U.S.C. 78l), or that is required to file reports under section 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78o(d)),

or any officer, employee, contractor, subcontractor, or agent of such company, may discharge, demote, suspend, threaten, harass, or in any other manner discriminate against an employee in the terms and conditions of employment because of any lawful act done by the employee—

"(1) to provide information, cause information to be provided, or otherwise assist in an investigation regarding any conduct which the employee reasonably believes constitutes a violation of section 1341, 1343, 1344, or 1348, any rule or regulation of the Securities and Exchange Commission, or any provision of Federal law relating to fraud against shareholders, when the information or assistance is provided to or the investigation is conducted by—

"(A) a Federal regulatory or law enforcement agency;

"(B) any Member of Congress or any committee of Congress; or

"(C) a person with supervisory authority over the employee (or such other person working for the employer who has the authority to investigate, discover, or terminate misconduct); or

"(2) to file, cause to be filed, testify, participate in, or otherwise assist in a proceeding filed or about to be filed (with any knowledge of the employer) relating to an alleged violation of section 1341, 1343, 1344, or 1348, any rule or regulation of the Securities and Exchange Commission, or any provision of Federal law relating to fraud against shareholders.

"(b) ENFORCEMENT ACTION.—

"(1) IN GENERAL.—A person who alleges discharge or other discrimination by any person in violation of subsection (a) may seek relief under subsection (c), by—

"(A) filing a complaint with the Secretary of Labor; or

"(B) if the Secretary has not issued a final decision within 180 days of the filing of the complaint and there is no showing that such delay is due to the bad faith of the claimant, bringing an action at law or equity for de novo review in the appropriate district court of the United States, which shall have jurisdiction over such an action without regard to the amount in controversy.

"(2) PROCEDURE.—

"(A) IN GENERAL.—An action under paragraph (1)(A) shall be governed under the rules and procedures set forth in section 42121(b) of title 49, United States Code.

"(B) EXCEPTION.—Notification made under section 42121(b)(1) of title 49, United States Code, shall be made to the person named in the complaint and to the employer.

"(C) BURDENS OF PROOF.—An action brought under paragraph (1)(B) shall be governed by the legal burdens of proof set forth in section 42121(b) of title 49, United States Code.

Deadline.

"(D) STATUTE OF LIMITATIONS.—An action under paragraph (1) shall be commenced not later than 90 days after the date on which the violation occurs.

"(c) REMEDIES.—

"(1) IN GENERAL.—An employee prevailing in any action under subsection (b)(1) shall be entitled to all relief necessary to make the employee whole.

"(2) COMPENSATORY DAMAGES.—Relief for any action under paragraph (1) shall include—

"(A) reinstatement with the same seniority status that the employee would have had, but for the discrimination;

"(B) the amount of back pay, with interest; and

"(C) compensation for any special damages sustained as a result of the discrimination, including litigation costs, expert witness fees, and reasonable attorney fees.

"(d) RIGHTS RETAINED BY EMPLOYEE.—Nothing in this section shall be deemed to diminish the rights, privileges, or remedies of any employee under any Federal or State law, or under any collective bargaining agreement.".

(b) CLERICAL AMENDMENT.—The table of sections at the beginning of chapter 73 of title 18, United States Code, is amended by inserting after the item relating to section 1514 the following new item:

"1514A. Civil action to protect against retaliation in fraud cases.".

SEC. 807. CRIMINAL PENALTIES FOR DEFRAUDING SHAREHOLDERS OF PUBLICLY TRADED COMPANIES.

(a) IN GENERAL.—Chapter 63 of title 18, United States Code, is amended by adding at the end the following:

"§ 1348. Securities fraud

"Whoever knowingly executes, or attempts to execute, a scheme or artifice—

"(1) to defraud any person in connection with any security of an issuer with a class of securities registered under section 12 of the Securities Exchange Act of 1934 (15 U.S.C. 78l) or that is required to file reports under section 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78o(d)); or

"(2) to obtain, by means of false or fraudulent pretenses, representations, or promises, any money or property in connection with the purchase or sale of any security of an issuer with a class of securities registered under section 12 of the Securities Exchange Act of 1934 (15 U.S.C. 78l) or that is required to file reports under section 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78o(d));

shall be fined under this title, or imprisoned not more than 25 years, or both.".

(b) CLERICAL AMENDMENT.—The table of sections at the beginning of chapter 63 of title 18, United States Code, is amended by adding at the end the following new item:

"1348. Securities fraud.".

White-Collar Crime Penalty Enhancement Act of 2002.

TITLE IX—WHITE-COLLAR CRIME PENALTY ENHANCEMENTS

18 USC 1341 note.

SEC. 901. SHORT TITLE.

This title may be cited as the "White-Collar Crime Penalty Enhancement Act of 2002".

SEC. 902. ATTEMPTS AND CONSPIRACIES TO COMMIT CRIMINAL FRAUD OFFENSES.

(a) IN GENERAL.—Chapter 63 of title 18, United States Code, is amended by inserting after section 1348 as added by this Act the following:

"§ 1349. Attempt and conspiracy

"Any person who attempts or conspires to commit any offense under this chapter shall be subject to the same penalties as those prescribed for the offense, the commission of which was the object of the attempt or conspiracy.

(b) CLERICAL AMENDMENT.—The table of sections at the beginning of chapter 63 of title 18, United States Code, is amended by adding at the end the following new item:

"1349. Attempt and conspiracy.".

SEC. 903. CRIMINAL PENALTIES FOR MAIL AND WIRE FRAUD.

(a) MAIL FRAUD.—Section 1341 of title 18, United States Code, is amended by striking "five" and inserting "20".

(b) WIRE FRAUD.—Section 1343 of title 18, United States Code, is amended by striking "five" and inserting "20".

SEC. 904. CRIMINAL PENALTIES FOR VIOLATIONS OF THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974.

Section 501 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1131) is amended—

(1) by striking "$5,000" and inserting "$100,000";

(2) by striking "one year" and inserting "10 years"; and

(3) by striking "$100,000" and inserting "$500,000".

28 USC 994 note.

SEC. 905. AMENDMENT TO SENTENCING GUIDELINES RELATING TO CERTAIN WHITE-COLLAR OFFENSES.

(a) DIRECTIVE TO THE UNITED STATES SENTENCING COMMISSION.—Pursuant to its authority under section 994(p) of title 18, United States Code, and in accordance with this section, the United States Sentencing Commission shall review and, as appropriate, amend the Federal Sentencing Guidelines and related policy statements to implement the provisions of this Act.

(b) REQUIREMENTS.—In carrying out this section, the Sentencing Commission shall—

(1) ensure that the sentencing guidelines and policy statements reflect the serious nature of the offenses and the penalties set forth in this Act, the growing incidence of serious fraud offenses which are identified above, and the need to modify the sentencing guidelines and policy statements to deter, prevent, and punish such offenses;

(2) consider the extent to which the guidelines and policy statements adequately address whether the guideline offense levels and enhancements for violations of the sections amended by this Act are sufficient to deter and punish such offenses, and specifically, are adequate in view of the statutory increases in penalties contained in this Act;

(3) assure reasonable consistency with other relevant directives and sentencing guidelines;

(4) account for any additional aggravating or mitigating circumstances that might justify exceptions to the generally applicable sentencing ranges;

(5) make any necessary conforming changes to the sentencing guidelines; and

(6) assure that the guidelines adequately meet the purposes of sentencing, as set forth in section 3553(a)(2) of title 18, United States Code.

(c) EMERGENCY AUTHORITY AND DEADLINE FOR COMMISSION ACTION.—The United States Sentencing Commission is requested to promulgate the guidelines or amendments provided for under this section as soon as practicable, and in any event not later than 180 days after the date of enactment of this Act, in accordance with the procedures set forth in section 219(a) of the Sentencing Reform Act of 1987, as though the authority under that Act had not expired.

SEC. 906. CORPORATE RESPONSIBILITY FOR FINANCIAL REPORTS.

(a) IN GENERAL.—Chapter 63 of title 18, United States Code, is amended by inserting after section 1349, as created by this Act, the following:

"§ 1350. Failure of corporate officers to certify financial reports

(a) CERTIFICATION OF PERIODIC FINANCIAL REPORTS.—Each periodic report containing financial statements filed by an issuer with the Securities Exchange Commission pursuant to section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m(a) or 78o(d)) shall be accompanied by a written statement by the chief executive officer and chief financial officer (or equivalent thereof) of the issuer.

"(b) CONTENT.—The statement required under subsection (a) shall certify that the periodic report containing the financial statements fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act pf 1934 (15 U.S.C. 78m or 78o(d)) and that information contained in the periodic report fairly presents, in all material respects, the financial condition and results of operations of the issuer.

"(c) CRIMINAL PENALTIES.—Whoever—

"(1) certifies any statement as set forth in subsections (a) and (b) of this section knowing that the periodic report accompanying the statement does not comport with all the requirements set forth in this section shall be fined not more than $1,000,000 or imprisoned not more than 10 years, or both; or

"(2) willfully certifies any statement as set forth in subsections (a) and (b) of this section knowing that the periodic report accompanying the statement does not comport with all the requirements set forth in this section shall be fined not more than $5,000,000, or imprisoned not more than 20 years, or both.".

(b) CLERICAL AMENDMENT.—The table of sections at the beginning of chapter 63 of title 18, United States Code, is amended by adding at the end the following:

"1350. Failure of corporate officers to certify financial reports.".

TITLE X—CORPORATE TAX RETURNS

SEC. 1001. SENSE OF THE SENATE REGARDING THE SIGNING OF CORPORATE TAX RETURNS BY CHIEF EXECUTIVE OFFICERS.

It is the sense of the Senate that the Federal income tax return of a corporation should be signed by the chief executive officer of such corporation.

TITLE XI—CORPORATE FRAUD ACCOUNTABILITY

Corporate Fraud Accountability Act of 2002.

SEC. 1101. SHORT TITLE. 15 USC 78a note.

This title may be cited as the "Corporate Fraud Accountability Act of 2002".

SEC. 1102. TAMPERING WITH A RECORD OR OTHERWISE IMPEDING AN OFFICIAL PROCEEDING.

Section 1512 of title 18, United States Code, is amended—

(1) by redesignating subsections (c) through (i) as subsections (d) through (j), respectively; and

(2) by inserting after subsection (b) the following new subsection:

"(c) Whoever corruptly—

"(1) alters, destroys, mutilates, or conceals a record, document, or other object, or attempts to do so, with the intent to impair the object's integrity or availability for use in an official proceeding; or

"(2) otherwise obstructs, influences, or impedes any official proceeding, or attempts to do so,

shall be fined under this title or imprisoned not more than 20 years, or both.".

SEC. 1103. TEMPORARY FREEZE AUTHORITY FOR THE SECURITIES AND EXCHANGE COMMISSION.

(a) IN GENERAL.—Section 21C(c) of the Securities Exchange Act of 1934 (15 U.S.C. 78u–3(c)) is amended by adding at the end the following:

"(3) TEMPORARY FREEZE.—

"(A) IN GENERAL.—

"(i) ISSUANCE OF TEMPORARY ORDER.—Whenever, during the course of a lawful investigation involving possible violations of the Federal securities laws by an issuer of publicly traded securities or any of its directors, officers, partners, controlling persons, agents, or employees, it shall appear to the Commission that it is likely that the issuer will make extraordinary payments (whether compensation or otherwise) to any of the foregoing persons, the Commission may petition a Federal district court for a temporary order requiring the issuer to escrow, subject to court supervision, those payments in an interest-bearing account for 45 days.

"(ii) STANDARD.—A temporary order shall be entered under clause (i), only after notice and opportunity for a hearing, unless the court determines that

notice and hearing prior to entry of the order would be impracticable or contrary to the public interest.

"(iii) EFFECTIVE PERIOD.—A temporary order issued under clause (i) shall—

"(I) become effective immediately;

"(II) be served upon the parties subject to it; and

"(III) unless set aside, limited or suspended by a court of competent jurisdiction, shall remain effective and enforceable for 45 days.

"(iv) EXTENSIONS AUTHORIZED.—The effective period of an order under this subparagraph may be extended by the court upon good cause shown for not longer than 45 additional days, provided that the combined period of the order shall not exceed 90 days.

"(B) PROCESS ON DETERMINATION OF VIOLATIONS.—

"(i) VIOLATIONS CHARGED.—If the issuer or other person described in subparagraph (A) is charged with any violation of the Federal securities laws before the expiration of the effective period of a temporary order under subparagraph (A) (including any applicable extension period), the order shall remain in effect, subject to court approval, until the conclusion of any legal proceedings related thereto, and the affected issuer or other person, shall have the right to petition the court for review of the order.

"(ii) VIOLATIONS NOT CHARGED.—If the issuer or other person described in subparagraph (A) is not charged with any violation of the Federal securities laws before the expiration of the effective period of a temporary order under subparagraph (A) (including any applicable extension period), the escrow shall terminate at the expiration of the 45-day effective period (or the expiration of any extension period, as applicable), and the disputed payments (with accrued interest) shall be returned to the issuer or other affected person.".

(b) TECHNICAL AMENDMENT.—Section 21C(c)(2) of the Securities Exchange Act of 1934 (15 U.S.C. 78u–3(c)(2)) is amended by striking "This" and inserting "paragraph (1)".

28 USC 994 note.

SEC. 1104. AMENDMENT TO THE FEDERAL SENTENCING GUIDELINES.

(a) REQUEST FOR IMMEDIATE CONSIDERATION BY THE UNITED STATES SENTENCING COMMISSION.—Pursuant to its authority under section 994(p) of title 28, United States Code, and in accordance with this section, the United States Sentencing Commission is requested to—

(1) promptly review the sentencing guidelines applicable to securities and accounting fraud and related offenses;

(2) expeditiously consider the promulgation of new sentencing guidelines or amendments to existing sentencing guidelines to provide an enhancement for officers or directors of publicly traded corporations who commit fraud and related offenses; and

(3) submit to Congress an explanation of actions taken by the Sentencing Commission pursuant to paragraph (2) and

any additional policy recommendations the Sentencing Commission may have for combating offenses described in paragraph (1).

(b) CONSIDERATIONS IN REVIEW.—In carrying out this section, the Sentencing Commission is requested to—

(1) ensure that the sentencing guidelines and policy statements reflect the serious nature of securities, pension, and accounting fraud and the need for aggressive and appropriate law enforcement action to prevent such offenses;

(2) assure reasonable consistency with other relevant directives and with other guidelines;

(3) account for any aggravating or mitigating circumstances that might justify exceptions, including circumstances for which the sentencing guidelines currently provide sentencing enhancements;

(4) ensure that guideline offense levels and enhancements for an obstruction of justice offense are adequate in cases where documents or other physical evidence are actually destroyed or fabricated;

(5) ensure that the guideline offense levels and enhancements under United States Sentencing Guideline 2B1.1 (as in effect on the date of enactment of this Act) are sufficient for a fraud offense when the number of victims adversely involved is significantly greater than 50;

(6) make any necessary conforming changes to the sentencing guidelines; and

(7) assure that the guidelines adequately meet the purposes of sentencing as set forth in section 3553 (a)(2) of title 18, United States Code.

(c) EMERGENCY AUTHORITY AND DEADLINE FOR COMMISSION ACTION.—The United States Sentencing Commission is requested to promulgate the guidelines or amendments provided for under this section as soon as practicable, and in any event not later than the 180 days after the date of enactment of this Act, in accordance with the procedures sent forth in section 21(a) of the Sentencing Reform Act of 1987, as though the authority under that Act had not expired. Deadline.

SEC. 1105. AUTHORITY OF THE COMMISSION TO PROHIBIT PERSONS FROM SERVING AS OFFICERS OR DIRECTORS.

(a) SECURITIES EXCHANGE ACT OF 1934.—Section 21C of the Securities Exchange Act of 1934 (15 U.S.C. 78u–3) is amended by adding at the end the following:

"(f) AUTHORITY OF THE COMMISSION TO PROHIBIT PERSONS FROM SERVING AS OFFICERS OR DIRECTORS.—In any cease-and-desist proceeding under subsection (a), the Commission may issue an order to prohibit, conditionally or unconditionally, and permanently or for such period of time as it shall determine, any person who has violated section 10(b) or the rules or regulations thereunder, from acting as an officer or director of any issuer that has a class of securities registered pursuant to section 12, or that is required to file reports pursuant to section 15(d), if the conduct of that person demonstrates unfitness to serve as an officer or director of any such issuer.".

(b) SECURITIES ACT OF 1933.—Section 8A of the Securities Act of 1933 (15 U.S.C. 77h–1) is amended by adding at the end of the following:

"(f) AUTHORITY OF THE COMMISSION TO PROHIBIT PERSONS FROM SERVING AS OFFICERS OR DIRECTORS.—In any cease-and-desist proceeding under subsection (a), the Commission may issue an order to prohibit, conditionally or unconditionally, and permanently or for such period of time as it shall determine, any person who has violated section 17(a)(1) or the rules or regulations thereunder, from acting as an officer or director of any issuer that has a class of securities registered pursuant to section 12 of the Securities Exchange Act of 1934, or that is required to file reports pursuant to section 15(d) of that Act, if the conduct of that person demonstrates unfitness to serve as an officer or director of any such issuer.".

SEC. 1106. INCREASED CRIMINAL PENALTIES UNDER SECURITIES EXCHANGE ACT OF 1934.

Section 32(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78ff(a)) is amended—

(1) by striking "$1,000,000, or imprisoned not more than 10 years" and inserting "$5,000,000, or imprisoned not more than 20 years"; and

(2) by striking "$2,500,000" and inserting "$25,000,000".

SEC. 1107. RETALIATION AGAINST INFORMANTS.

(a) IN GENERAL.—Section 1513 of title 18, United States Code, is amended by adding at the end the following:

Penalties.

"(e) Whoever knowingly, with the intent to retaliate, takes any action harmful to any person, including interference with the lawful employment or livelihood of any person, for providing to a law enforcement officer any truthful information relating to the commission or possible commission of any Federal offense, shall be fined under this title or imprisoned not more than 10 years, or both.".

Approved July 30, 2002.

LEGISLATIVE HISTORY—H.R. 3763 (S. 2673):

HOUSE REPORTS: Nos. 107–414 (Comm. on Financial Services) and 107–610 (Comm. of Conference).

SENATE REPORTS: No. 107–205 accompanying S. 2673 (Comm. on Banking, Housing, and Urban Affairs).

CONGRESSIONAL RECORD, Vol. 148 (2002):

Apr. 24, considered and passed House.

July 15, considered and passed Senate, amended, in lieu of S. 2673.

July 25, House and Senate agreed to conference report.

WEEKLY COMPILATION OF PRESIDENTIAL DOCUMENTS, Vol. 38 (2002):

July 30, Presidential remarks and statement.

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InfoPAK

In-house Counsel Standards Under Sarbanes-Oxley

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In-house Counsel Standards Under Sarbanes-Oxley

The following material is intended to provide useful information and resources to help attorneys navigate through the attorney standards mandated by the Sarbanes-Oxley Act of 2002 and the specific rules issued by the Securities and Exchange Commission ("SEC Rules") on January 23, 2003. By examining the key interpretations of 17 C.F.R. pt. 205 that apply to attorney conduct, this InfoPAK helps define the scope and potential applications of the law by identifying which lawyers are governed by the standards and exploring the type of corporate conduct likely to trigger the Act's new obligations. This information should not be construed as legal advice or legal opinion on specific facts, or representative of the views of ACC or any of its lawyers, unless so stated. This is not intended as a definitive statement on the subject but a tool, providing practical information for the reader.[1]

We hope that you find this material useful. Thank you for consulting with the Association of Corporate Counsel.

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I. Introduction

Congress introduced the Sarbanes-Oxley Act of 2002[2] during a flurry of corporate debacles and public controversy. Companies such as Enron and WorldCom faced unprecedented legal and accounting challenges when investors filed actions for securities fraud against the corporations and their executives. Corporate executive officers, accountants, and lawyers were among the named defendants indicted for concealing financial information, inflating the company stock and other accounting fraud.[3] Meanwhile, a central issue moved through the public landscape regarding the role of lawyers in such scandals and the possible failure of states to adequately regulate these concerns. In response, Congress passed a wide-ranging corporate governance and accounting oversight bill through both houses by an overwhelming majority.[4] Sarbanes-Oxley, as it is so called, affects accountants, corporate executives, shareholders, and lawyers alike. Importantly, Section 307 of the Act requires the Securities and Exchange Commission ("SEC" or "the Commission") to issue new standards for attorneys.[5]

The Securities and Exchange Commissions, pursuant to the Sarbanes-Oxley Act, adopted 17 C.F.R. pt. 205 ("SEC Rules") on January 29, 2003,[6] which prescribes standards of professional conduct for all attorneys who appear and practice before the SEC in the representation of public company issuers. Functionally, the SEC Rules, which became effective on August 5, 2003, provide standards and procedures for "up the ladder" reporting of corporate misconduct.

Prior to the Sarbanes-Oxley Act, the SEC possessed authority to discipline attorneys appearing before it that had a role in false and misleading statements; however, this power was rarely exercised. In early 2002, a group of professors urged the SEC to use this power to impose a rule on "up the ladder" requirements, but the SEC declined to do so on the basis that the ethical responsibility of attorneys was a matter for the state to regulate.[7] Traditionally, ethical standards involving the legal profession were a matter of state regulation, set forth by either the courts or state bar authorities. Today, it would seem that the SEC rules do not preempt state law entirely,[8] as the SEC has announced that states are free to impose more rigorous ethical standards for attorneys than those prescribed in the SEC Rules.[9] Yet, administrative law jurisprudence establishes that agency rules prevail when in conflict with state laws.[10] As such, even after reviewing the SEC rules and applicable state law, attorneys will need to judge for themselves whether the SEC's effort to override conflicting state rules is effective.

Historically, two relevant principles were reflected in the ABA Model Rules of Professional Conduct: (1) the duty to maintain client confidences, except in order to prevent death or substantial bodily harm[11] and (2) the lawyer for a corporation represents the corporation acting through its duly authorized constituents and not the Board members, directors or principals individually.[12] Thus, the traditional view regarding a lawyer's duty to take action where a lawyer knows of possible

illegal activity could be interpreted to actually discourage such internal action. Although the ABA refused to modify the Model Rules of Professional Conduct in 2000 to include cases of economic harm as an "exception" to the confidentiality rule, the new 2002 ABA task force recommended these rules.[13] The ABA finally amended its rules in August of 2003 to codify this exception. Today, the new rules largely embody language similar to that contained in the SEC Rules.[14]

Lawyers are being hired for their business management experience and are being used to ensure that their employer is meeting the more stringent requirements of the Sarbanes-Oxley Act of 2002.[15]

In part because of the duty to report up-the-ladder and, if necessary, outside the organization, corporate attorneys necessarily have increased responsibility and obligations. In addition to the previous burdens associated with serving as in-house counsel, corporate attorneys must develop and demonstrate knowledge and independent leadership over regulatory compliance and internal codes of conduct. It should be expected that conflicts between the corporation's officers and lawyers may arise under the atmosphere inherent in the Sarbanes-Oxley and the ABA Model Rules requirements. Counsel, hired by management to advise and ultimately to aid the client to make business judgments, may now be seen as opposing the company's directors and officers! Management may fear that up-the-ladder and outside the organization reporting will lead to situations where the attorney undermines the client's decision by illuminating problematic situations that previously would be viewed as business decisions only. Similarly, counsel will perceive the additional reporting requirements as an impediment to the free flow of information between management and the legal counsel's office.

The rules promulgated by the SEC in light of Sarbanes-Oxley, along with Model Rule 1.13, will increase the obligations of corporate attorneys while potentially decreasing the access of in-house counsel to information necessary to meet those same obligations. On top of the SEC and Model rules, in-house attorneys should also look to applicable state law on attorney-client privilege, as the regulation varies in each state. To access the new ABA rules, see:

- ACCA Release, American Bar Association's Revised Model Rules of Professional Conduct 1.6 & 1.13 (August 20, 2003), at: http://www.acca.com/protected/comments/professionalconduct.pdf

For additional history on professional codes of conduct and industry self-regulation, see:

- Gretchen A. Winter, David J. Simon, Code Blue, Code Blue: Breathing Life into Your Company's Code of Conduct, ACCA Docket 20 v.10 (November/December 2002): 72-89, available at: http://www.acca.com/protected/pubs/docket/nd02/codeblue2.php

- H. Barnes, An Economic History Of The Western World (1942).
- A. Black, Guilds And Civil Society In European Political Thought From The Twelfth Century To The Present (1983).
- R. Heilbroner, The Making Of Economic Society (1980).
- Kidder, Is Society Entering a New 'Age of Ethics'? Christian Science Monitor, October 19, 1987, at 19.
- Washington Metropolitan Area Corporate Counsel Association, Understanding the New SEC Attorney Responsibility Rules (February 6, 2003), available at: http://www.acca.com/chapters/program/wmacca/307rules.pdf.
- Practical Tips for Dealing with the New Attorney Responsibility Standards," Article Sidebar, ACC Docket 21, no. 5(May 2003): 40-55, available at http://www.acca.com/protected/pubs/docket/mj03/standard_tips.php.
- Steven N. Machtinger and Dana A. Welch, In-house Ethical Conflicts: Recognizing and Responding to Them, ACC DOCKET 22, no. 2 (February 2004).
- Dongju Song, The Laws of Securities Lawyering Under Sarbanes-Oxley, 53 Duke L.J. 257 (2003).
- Jenny E. Cieplak and Michael K. Hibey, Sarbanes-Oxley Regulations and Model Rule 1.13: Redundant or Complimentary, GEOJLE (Summer 2004).
- Jay K. Musoff and Adam S. Zimmerman, Ethics and Off-Switches: What Next? The Tyco Mess Offers an Opportunity to Look and the Changing Role of the GC, Legal Times, vol. 27, no. 38 (September 20, 2004).

II. Who is Affected by the Rules?

The Sarbanes-Oxley Act regulates corporate governance by setting minimum standards of professional conduct in the interest of protecting investors. As mentioned in the above section, Section 307 of the Act applies directly to attorneys, as it directs the Commission to establish professional standards that govern attorneys "appearing and practicing" before the SEC on behalf of their company clients. The SEC Rules, which took effect on August 5, 2003, require attorneys to report evidence of certain material violations including, but not limited to, breach of fiduciary duty committed by their corporate client, "up the ladder" within the organization. The SEC rules were meant to supplement standards of professional conduct developed by the individual states. Rather than limit the states from imposing additional regulations (so long as they were not inconsistent with the SEC rules). Where state standards conflict with SEC regulations though, the SEC rule will preempt the state standard.[16]

A. Attorneys Governed by the Sarbanes-Oxley Act

In broad terms, the Sarbanes-Oxley Act requires the SEC to regulate the conduct of attorneys "appearing and practicing before the Commission in any way in the representation of the issuers."[17] The SEC now expects attorneys, whether in-house or outside counsel to serve as "gatekeepers in maintaining fair and honest markets."[18]

Fortunately, the SEC has provided more detail on the scope of the law and its application to attorneys in adopting 17 C.F.R. pt. 205.[19] The definitions reveal that the scope is wider than it may appear on its face:

- **Attorneys:** Any person licensed or otherwise qualified to practice law in any jurisdiction with the exception of "non-appearing" foreign attorneys.[20]

- **Issuer:** A person who issues (or proposes to issue) registered securities under the Securities Act of 1933,[21] OR is required to file with the SEC under the Act,[22] OR that files or has filed a registration statement that has not yet become effective under the Act AND that has not been withdrawn.[23] According to the SEC rule, the term "issuer" also includes any person controlled by an issuer, such as a subsidiary, when provided at the behest, or for the benefit of, the issuer even if the attorney is not employed or retained by the issuer.[24] It is unclear from the rule as to when an attorney representing a subsidiary would be deemed to be acting for the issuer.[25] "Issuer" excludes a foreign government issuer.

- **Appears and practices before the SEC in any way:** Under §§ 205.2 (a), 205.3 (b)(5) and 205.4 (b), the range of activity includes an attorney who engages in any of the following activities:[26]

Transacts business with the SEC, including communications in any form.

Represents a company in a SEC administrative proceeding or in connection with any SEC investigation, inquiry, information request, or subpoena.

Provides advice with respect to the federal securities laws regarding any document that the attorney has notice will be filed with or submitted to or incorporated into any document that will be filed with or submitted to the SEC.

Advises the company as to whether information or a statement is required to be filed with or submitted to the SEC or incorporated into a document that is filed with or submitted to the SEC.

Conducts an investigation on behalf of the company pursuant to Part 205.

Supervises and directs an attorney who is appearing and practicing before the SEC in the representation of an issuer.

Further, the SEC establishes that these activities must be undertaken within the context of providing legal services to a company, with whom the attorney has an attorney-client relationship, even though the communications would not be protected by the attorney-client privilege. Hence, if the attorney were only acting in a partial legal capacity, as long as the attorney was providing legal services, s/he would be governed by the law.[27]

- **In the representation of issuers:** The rules provide that attorneys who fall within the ambit of the law are those who represent issuers.[28] The SEC standards further define this type of representation to include "providing legal services as an attorney for an issuer, regardless of whether the attorney is employed or retained by the issuer."[29] The rules state that an attorney represents the issuer as an organization, however, not the issuer's individual officers or employees.[30] Hence, the rule only covers an attorney who is providing legal advice to an issuer where there is an attorney-client relationship. Attorneys for third parties who review part of an issuer's disclosure document or render a legal opinion to an issuer who is not their client are not covered by the rules.
  However, attorneys can become subject to the rules even though they do not counsel the issuer in two instances. First, an attorney employed by an investment adviser who prepares material for an investment company knowing it will be filed with the SEC will fall within the ambit of the rules, on the basis that such conduct falls squarely within the definition of "appearing and practicing" before the Commission. Second, an attorney for a controlled subsidiary can be deemed appearing and practicing before the Commission in the presentation of the parent, as the term "issuer" is defined to include a person controlled by the

issuer.
It is also important to note that once an attorney becomes subject to the rules with respect to an issuer, the material violation that must be reported need not relate to the matter that placed the attorney within the ambit of the law.

The SEC's definition of "appearing and practicing" seems to widen the potential scope of attorneys to which the law applies. For example, a non-securities specialist who prepares or reviews a discrete section of a disclosure document could be deemed to have appeared or practiced before the SEC. An attorney who prepares an agreement that the attorney knows will be filed as an exhibit to a SEC filing may similarly be subject to the rules under certain circumstances. Hence, it is not surprising that many corporations have instructed all attorneys admitted to practice within the U.S. within the general counsel's office to assume they fall within reach of the SEC standards.[31]

For additional discussion on how to interpret "appearing and practicing before the commission," and the extent to which attorneys fall within the ambit of the Sarbanes-Oxley Act, see:

- Laurence Stuart, In-House Counsel as Corporate Cop–Up the Ladder or Down the Chute, (Baker & McKenzie 2003), available at: http://www.acca.com/protected/legres/ethics/corpcop.pdf
- Abba David Poliakoff, A Trap for the Unprivileged: New SEC Attorney Conduct Rules, 37-Feb MDBJ 8, 10 (2004).
- Broc Romanek and Kenneth B. Winer, The New Sarbanes-Oxley Attorney Responsibility Standards, ACCA Docket 21, no.5 (May 2003): 40-55, available at: http://www.acca.com/protected/pubs/docket/mj03/standard1.php
- John Olson, Jonathon Dickey, et al., Recent Developments in Federal Securities Regulations of Corporate Finance as of July 22nd 2004, 2004 ACC Annual Meeting (Oct. 2004), available at: www.acca.com/am/04/
- John Villa, A First Look at the Final Sarbanes-Oxley Regulations Governing Corporate Counsel, ACCA Docket 21, no. 4 (April 2003):90-99 , available at: http://www.acca.com/protected/pubs/docket/am03/ethics2.php
- Washington Metropolitan Area Corporate Counsel Association: Understanding the New SEC Attorney Responsibility Rules (February 6, 2003), at: http://www.acca.com/chapters/program/wmacca/307rules.pdf

To access the legislative and administrative materials online, see:

- Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745, Section 307 (2002), available at: http://www.acca.com/legres/enron/sarbanesoxley.pdf

- Securities and Exchange Commission Final Rule: Implementation of Standards of Professional Conduct for Attorneys, 17 C.F.R. pt. 205 (2002), available at: http://www.sec.gov/rules/final/33-8185.htm
- Securities and Exchange Commission Proposed Rule: Implementation of Standards of Professional Conduct for Attorneys, Release No. 33-8186 (Jan. 29, 2003), available at: http://www.sec.gov/rules/proposed/33-8186.htm
- See www.seclaw.com/secrules.htm for an online version of many securities law statutes, regulations and forms.

B. Outside Counsel Versus In-house Attorneys: Are the Duties the Same?

Since Part 205 of the SEC Rules establishes standards of professional conduct for all attorneys who appear and practice before the SEC in the representation of public issuers, the regulation includes outside attorneys. Thus, under the SEC's new attorney standards, outside counsel incur the same obligations as in-house counsel. There is certainly no one-size-fits-all answer or bright line test to answer the question of when the duty arises. In-house and outside counsel instead must rely on their best judgment and the rules laid out by the SEC on the matter.[32]

Outside firms can play a pivotal role in providing their clients guidance on the SEC Rules. For sample memos to corporate clients, see:

- Letter to Outside Counsel, Thomas Gottschalk, Executive Vice President Law & Public Policy & General Counsel, General Motors, at: http://www.acca.com/protected/policy/conduct/gm_ocletter.pdf
- Memo to Clients and Other Interested Parties, O'Melveny & Myers LLP (February 24, 2003), at: http://www.acca.com/chapters/socal/program/sox/attorney_conduct_rules.pdf
- Washington Metropolitan Area Corporate Counsel Association, Understanding the New SEC Attorney Responsibility Rules (February 6, 2003), at: http://www.acca.com/chapters/program/wmacca/307rules.pdf

For information on how to use outside firms to help your legal department navigate through the new attorney standards, see:

- Richard Ober and Michael Parish, Maybe You Need a Lawyer: Does the Sarbanes-Oxley Act Make the SEC Your Client? ACC Docket 21, no. 4 (April 2003): 70-85, available at: http://www.acca.com/protected/pubs/docket/am03/client1.php

For more information on ethics and professional issues related to Sarbanes-Oxley

as tied to the role of in-house and outside counsel, see:

- Role of the General Counsel, ACC InfoPAK (March 2005), available at www.acca.com/protected/infopaks/role_gc/infopak.pdf
- Kathryn M. Fenton, Counseling the Corporation Post-Sarbanes-Oxley: Ethics and Professionalism Issues for In-house and Outside Counsel, 2004, available at: www.acca.com/protected/legres/corpresp/counselingcorporation.pdf

Corporations have drafted policies and procedures for outside counsel in satisfying its obligations under Part 205 of the SEC Rules. These revised corporate policies are intended to supplement, not restate the SEC requirements, as the drafters expect that outside counsel will familiarize themselves with the SEC Rules. The following are model corporate policies and procedures for outside counsel:

- Model Letter to Outside Counsel Regarding Compliance with SEC Rule 205, Wilmer, Cutler & Pickering, at: http://www.acca.com/protected/policy/conduct/wilmer_ocpolicy.pdf
- Policy Regarding Compliance with SEC Attorney Conduct Rules, at page 12, at: http://www.acca.com/protected/policy/conduct/rules_sample1.pdf

III. When Does the Duty Arise?

A. Overview

A significant attorney duty imposed by the SEC standards pursuant to Section 307 of the Act is presented in an extensive scheme requiring an attorney who becomes aware of "evidence of a material violation" (as an appearing and practicing attorney before the SEC in the representation of a company), to report that evidence "up the ladder." Specifically, the SEC Rules require an attorney to:

1. report evidence of a material violation of securities law or breach of fiduciary duty (or other similar act) to the Chief Legal Officer (CLO) or Chief Executive Officer (CEO)[33]

and

2. if the CEO or CLO fails to respond appropriately to such evidence to the: Audit Committee of Board of Directors (or another committee of non-employee directors) or the Board of Directors if there is no audit committee.[34]

However, counsel needs to understand the circumstances that trigger this requirement under the SEC rules. Then, counsel must become familiar with the prescribed methods for reporting up the ladder.

B. When is the Duty to Report "Up the Ladder" Triggered?

Again, "attorney" in this context refers to one appearing and practicing before the SEC in the representation of a company. Once a lawyer is deemed to fall within the reach of the regulations, his or her duty is set forth in Section 205.3(b)(1)[35]:

"[i]f an attorney… becomes aware of evidence of a material violation by the issuer or by any officer, director, employee or agent of the issuer, the attorney shall report such evidence to the issuer's chief legal officer… or to both the issuer's chief legal officer and its chief executive officer… forthwith…"[36]

Thus, the duty to report under the SEC rules is triggered when a lawyer becomes "aware of evidence of material violation by a company or its officer, director, employee, or agent." The rule itself does not specify any required quantum, proportion, or persuasive effect of the evidence. Yet, the rule further explains that such evidence includes "credible evidence, based upon which it would be unreasonable, under the circumstances, for a prudent and competent attorney not to conclude that it is reasonably likely that a material violation has occurred, is ongoing, or is about to occur."[37] Further, the rules and adopting release define these terms as follows:

- **Circumstances** are relevant circumstances, including the reporting attorney's experience, expertise, and knowledge.[38] These also includes the time constraints under which the attorney is acting, the attorney's previous experience and familiarity with the client, and the availability of other lawyers with whom the attorney may consult. [39]
- **Material violation** is a violation of an applicable U.S. state or federal securities law, a material breach of fiduciary duty arising under a state or federal law, or similar material violation of any state statutory or common law, or federal law.[40] Although the Commission did not define "material" in the rules, the release notes that the term material should be interpreted by the courts in light of its usual meaning under the applicable federal securities law.[41]
- **Reasonably likely knowledge requirement** demands that a material violation must be more than merely possible, but need not be "more likely than not."[42]
- **Breach of fiduciary duty** is committed by any breach of fiduciary duty (or similar duty), recognized by federal or state law, to a company including but not limited to: misfeasance, nonfeasance, abdication of duty, abuse of trust, and approval of unlawful transactions.[43] It remains unclear if all duties of diligence,

care and loyalty are subject to the rule.

Both the ABA Model Rule and SEC Rule 205.3(b)(1) contain this mandatory up-the-ladder reporting requirement. The Model Rules requires that if a lawyer for an organization knows that an organization's agent is engaged in actions which will harm the company or violate the law in a manner that will cause substantial injury to the client, that lawyer must report it to any higher authority in the organization. The SEC Rule is also mandatory, but refers to these same violations that must be reported as "material violations" instead of those that will cause substantial harm. The SEC Rules attempt to provide greater content and clarity to the reporting requirements than the ABA Model Rules.

C. Issues Presented

(1) Compare Standard to Rule 1.13 of the ABA Model Rules of Professional Conduct

Although the SEC rules only apply to attorneys practicing before the Commission, those states that have adopted Model Rule 1.13 impose substantially the same requirements upon all attorneys. The main difference between the SEC Rule and the state ethics rules is the mechanism of enforcement. Where the Model Rules are enforced through state processes, the SEC rules are enforced by the Commission itself.[44]

The SEC has stated that where the state-adopted ABA Model Rule differs from the standards established in the SEC final rules, the SEC standards will prevail.[45] An important distinction in interpreting which lawyers are within the scope of Sarbanes-Oxley is that the SEC standards require an in-house lawyer to take action, including reporting up the ladder, when the lawyer becomes aware of any evidence of a material violation. Model Rule 1.13, by contrast, requires the attorney to take action only when the attorney learns of certain facts related to his or her representation.[46] Thus, a lawyer under Model Rule 1.13 must act only if he or she has reached a high level of certainty (knows) that a violation has occurred. The SEC's commentary explains that it had rejected the knowing requirement for the "reasonably likely" standard.[47] It also describes the "reasonably likely" standard as "more than a mere possibility but it need not be 'more likely than not.' "[48] Such a loose standard will certainly prove difficult, as attorneys struggle to apply it to factual scenarios in the future. Further, Model Rule 1.13 merely suggests that in-house lawyers may report up the ladder upon receiving evidence of their client's wrongdoing, while Sarbanes-Oxley mandates such action.

Meanwhile, practitioners believe that state bar associations are likely to raise the bar on attorney conduct by modifying Rule 1.13 and other corresponding Sarbanes-Oxley rules.[49] However, since the revised Model Rules of Professional Conduct failed to seize the opportunity to reconcile these differences, it is doubtful the states will take the initiative. Additional issues regarding Rule 1.13 and confidentiality are analyzed in subsequent sections.

For more discussion as well as practical advice concerning these reporting up the ladder issues, the following sources may be helpful:

- Memo Regarding What Legal Departments Can Do to Prepare for Compliance with New SEC Rules, ACCA Memo, available at: http://www.acca.com/protected/article/corpresp/8krule.pdf
- Thomas Lee Hazen, Administrative Law Controls on Attorney Practice: A Look at the Securities and Exchange Commission's Lawyer Conduct Rules, 55 admlr 323 (2003).
- Giovanni P. Prezioso, Public Statement by SEC Official: Letter Regarding Washington State Bar Association's Proposed Opinion on the Effect of the SEC's Attorney Conduct Rules, Gen. Couns. Mem. (July 23, 2003), available at:
- www.sec.gov/news/speech/spch072303gpp.htm
- John K. Villa, A First Look at the Final Sarbanes-Oxley Regulations Governing Corporate Counsel, ACCA Docket 21 no. 4(April 2003): 90-99, available at: http://www.acca.com/protected/pubs/docket/am03/ethics2.php
- Jenny E Cieplak, Michael K. Hibey, The Sarbanes-Oxley Regulations and Model Rule 1.13: Redundant or Complementary, The Georgetown Journal of Legal Ethics, (Summer 2004).
- Reporting Up the Ladder: Unclear Case Law Creates Tough Decisions, Corporate Legal Times, vol. 15, no. 163 (June 2005).

For discussion of preemption issues, see:

- Chi Soo Kim and Elizabeth Laffittee, The Potential Effects of SEC Regulation of Attorney Conduct Under the Sarbanes-Oxley Act, 16 Geojle 707 (2003).

(2) Material Breach of Fiduciary Duty

The SEC definition of "material violation" will certainly cause confusion, as it extends the triggering factor for its reporting requirement to a breach of fiduciary duty including a "similar duty." Some experts observe that attorneys are not necessarily well suited to judge the behavior of corporate management, especially in deciding on such issues as whether a manager has breached a duty of care. A duty of care, in corporate terms, involves a balance of risk and return, a task tradition-

ally relegated to corporate management, not lawyers. In fact, the role of a lawyer in judging management's duty is inconsistent with the ABA Model Rules (namely 1.13—"up the corporate ladder" rule), which provides that "[w]hen constituents of the organization make decisions for it, the decisions ordinarily must be accepted by the lawyer even if their utility or prudence is doubtful. Decisions concerning policy and operations, including ones entailing substantial risk, are not as such in the lawyer's province."[50] Placing the responsibility of judging whether management has breached its duty of care upon lawyers, some assert, invites much confusion and trouble.

For a discussion on possible issues surrounding the SEC Rules, particularly on attorney standard of knowledge for reporting and identifying breach of duties, the following articles may be insightful:

- Guidelines Regarding SEC Standards of Professional Conduct for Attorneys, Palmer & Dodge LLP, at: http://www.acca.com/protected/policy/conduct/palmerdodge.pdf
- Securities and Exchange Commission Final Rule: Implementation of Standards of Professional Conduct for Attorneys, 17 C.F.R. pt. 205 (2002), available at: http://www.sec.gov/rules/final/33-8185.htm

For additional resources interpreting key phrases in Part 205 of the SEC standards, see:

- Laurence Stuart, In-house Counsel as Corporate Cop–Up the Ladder or Down the Chute, (Baker & McKenzie 2003), available at: http://www.acca.com/protected/legres/ethics/corpcop.pdf
- John K. Villa, A First Look at the Final Sarbanes-Oxley Regulations Governing Corporate Counsel, ACCA Docket 21, no. 4 (April 2003): 90-99, available at: http://www.acca.com/protected/pubs/docket/am03/ethics2.php

IV. Reporting Obligations in the Event of Material Violation: Implementing the "Up the Ladder" Requirement

A. Reporting Attorney's Duties

The "up the ladder" duty requires an attorney to report evidence of a material violation to either a supervisory attorney, or the company's chief legal counsel, or chief executive officer. The CEO or CLO, not the reporting attorney, must conduct an inquiry. When the attorney chooses to report such evidence directly to the company's CEO or CLO, she must assess whether the officer responded appropriately. If the attorney does not believe the response from the corporate officer was appropriate, she must report the violation up to the issuer's audit or other independent committee or to the full board of directors. The standards allow an attorney to report directly to the committees or board, if he or she feels that it would be futile to report to the CEO or CLO.

A reporting attorney who receives an appropriate and timely response to his/her report will have satisfied the obligations under the rules. Note that the rules do not impose a separate duty on the reporting attorney to investigate the evidence of a material violation. However, an attorney who has reported the matter all the way "up the ladder" and has not received an appropriate and timely response must explain his reasons for this belief to either the CLO, CEO, Board of Directors, audit or independent committee to whom he reported the evidence of a material violation.

B. Supervisory Attorney's Duties

The "up the ladder" reporting duty requires an attorney to turn in evidence of a material violation to either a supervisory attorney, or the company's chief legal counsel (CLO), or chief executive officer (CEO). If the reporting attorney chooses to report to a supervisory attorney, the supervisory attorney must then assess whether a material violation has occurred, is ongoing, or is about to occur. If the supervisory attorney does not reasonably believe that there is a material violation (or potential violation), then he or she must notify the subordinate attorney of this conclusion. The subordinate attorney may then decide whether to report the evidence to the CLC or CEO, the company's board or audit committee, or other independent committee of the corporation. However, the subordinate attorney is not required to do so. If the supervisory attorney believes that there is credible evidence of a material violation, he or she must report such evidence up the ladder

to the company's chief legal or executive officer.

The duty of the attorney reporting the matter to the CLO or CEO is not complete at this point. Rather, he or she must evaluate the response from the issuer's chief legal or executive officer. If the reporting attorney feels the officer has not appropriately responded to the concern, he or she must report directly to the company's audit committee, the board of the directors, or another committee of independent directors.

It may be argued that Rule 205 requires no more of lawyers than what most would already do – that is, move issues up the ladder within an organization and seek an appropriate response. However, it is also true that the trigger for the reporting obligation in the rule is inherently ambiguous. The standard is that lawyers must be "aware" of evidence of a material violation. But, how does one define that point in time when they become "aware" of something? And how much evidence of a material violation is required? For example, if an employee or officer forwards in-house counsel an e-mail containing a rumor of bad acts, is the attorney then "aware" of a material violation? What happens when a disgruntled employee of suspect credibility brings a potential problem to the attention of in-house counsel?[51]

The importance of adhering to the new standards was illustrated by the SEC's case against John E. Isselman, Jr., the former General Counsel of Electro Scientific Industries Inc. (ESI). In September 2004, the SEC charged Isselman with a violation of Rule 13(b)2-2 of the Exchange Act for failing to provide important information to ESI's audit committee, board of directors and auditors regarding a significant fraudulent accounting transaction that enabled ESI to report a profit rather than a loss. The SEC did not allege that Isselman participated in the scheme to boost profits, nor that he knew about the fraud. However, the SEC determined that Isselman's failure to report the transaction up the ladder after he learned of the fraud constituted a violation of securities law. In his settlement with the SEC, Isselman did not admit or deny the agency's allegations but he did agree to pay a $50,000 civil penalty and agreed to a cease-and-desist order.

In January 2005, the SEC charged Google and its General Counsel, David C. Drummond, with failure to register over $80 million in employee stock options.[52] The federal securities laws require companies issuing over $5 million in options during a 12 month period to provide detailed financials to recipients or register—thereby publicly disclosing financial and other information. The commission further found that Drummond was aware that the registration and related disclosure obligations had been triggered, but believed Google could avoid providing the information to its employees by relying on an exemption from the law. The exemption was, in fact, inapplicable.

In order to comply with the Section 307 rules, many companies have developed written policies or standards describing their "up-the-ladder" reporting expectations. These expectations should be communicated to (and apply to) all attorneys

within a company and reportable allegations covered by departmental policies may be broader in scope and application than the SEC rules may require. Most company policies do not want in-house counsel to deliberate as to whether they should report something wrong to the CLO or other senior counsel. Rather, they want allegations of wrongdoing reported up within the legal department immediately. Although individual companies' procedures may vary, most will include the creation of internal guidance resources and extensive training. Many legal departments have a designated advisory counsel or committee to assist attorneys who are confused or need advice.

C. The Duties of the Chief Legal Officer ("CLO") & the Chief Executive Officer ("CEO")

If the reporting or supervisory attorney decides to report to the CEO or CLO of the company, that officer must then conduct reasonable inquiry into the possible violations outlined in the report. If either officer determines no material violation has occurred, is ongoing or is about to occur, it must notify the reporting attorney of such findings and state the basis for such an opinion.

If the CLO finds that there is a material violation, the CLO must take reasonable steps to cause the company to stop the violations, to prevent it, or to remedy the consequences of the violation. A CLO may want to launch an inquiry or turn the matter over to a legal compliance committee. However, the compliance committee must have been established before the event occurred. [53]

On July 15, 2004, Mark Belnick, the former General Counsel for Tyco International Ltd. was acquitted of charges of grand larceny, securities fraud, and falsifying business records for accepting more than $30 million in the form of unauthorized loans and bonuses. The central defense argument throughout the case was that the prosecution's case was based on a fundamental misunderstanding of the GC's role in ferreting out corporate fraud. The prosecution alleged that Belnick must have known about Tyco's misdeeds and that the failure to uncover and disclose irregularities in his $30 million compensation package was part of a cover-up. However, according to the defense, Belnick was entitled to rely on the word of the CEO and CFO for guidance on issues of board approval and compensation. Although a jury ultimately acquitted Belnick, his trial came at a significant personal and professional cost. The Belnick case illustrates the importance of the GC's need to have internal controls that ensure that good information reaches the top of the ladder in light of changing professional rules and changing perceptions of those rules. As GCs assume a greater responsibility for being aware of what is going on in their organizations, there is an increased possibility that more information, and less meaningful information, will be reported up to ladder to them.[54]

D. Determining Whether the Response is "Appropriate"

The SEC identifies three possible responses an attorney may receive that are considered appropriate. Hence, the phrase, "appropriate response" means a response that provides a basis for an attorney to reasonably believe that:

- there is no occurring material violation,
- the company has adopted appropriate remedial measures (including taking appropriate steps or sanctions to stop any material violations that are ongoing, to prevent any material violation that has yet to occur, and to remedy or otherwise appropriately address any material violation that has already occurred and to minimize the likelihood of its recurrence), or
- the company, with the consent of the board (or other independent committee or a QLCC), has retained or directed an attorney to review the reported evidence of a material violation and has either implemented the attorney's remedial recommendations or been advised by the attorney that he or she can assert a colorable defense in any proceeding relating to the reported violation.[55]

Note that the third approach requires only that the reporting attorney and CLO form a reasonable belief that the company retained or directed an attorney to take action. This will likely reduce the burden of the company to furnish substantial information to the reporting attorney, particularly if the reported violation is beyond the scope of the attorney's expertise. In contrast, the first two options require the reporting attorney to form a reasonable belief as to whether a material violation exists and whether the response was appropriate. Further, under the third approach, the reporting attorney and CLO or CEO will be less exposed to being second-guessed by the SEC.[56]

For guidance and information on up the ladder reporting and checklists, see:

- Attorney-Client Privilege in the Corporate Setting, Fact Sheet, Quinn Emanuel Urquhart Oliver & Hedges, LLP, available at: http://www.acca.com/chapters/socal/program/corpattyclient.pdf
- Broc Romanek and Kenneth Winer, The New Sarbanes-Oxley Responsibility Standards, Feature Article, ACCA Docket 21 no. 5 (May 2003): 40-55, available at: http://www.acca.com/protected/pubs/docket/mj03/standard1.php
- Sample General Counsel Letter to Legal Department regarding Sarbanes-Oxley "Up the Ladder" Reporting, available at: http://www.acca.com/protected/forms/corpresp/jci_qlcc.pdf

Summary: The Final Rule: Responsibilities of Supervisory and Subordinate Attorneys[57]

- The rules define a "supervisory attorney" (e.g., a CLO in a public company or a partner in an outside law firm) as an attorney who directs or supervises one or more subordinate attorneys.
- A "subordinate attorney" does not include one who is under the direct supervision or direction of the CLO.
- To the extent a subordinate attorney appears and practices before the SEC, that attorney's supervisory attorneys are deemed also to appear and practice before the SEC.
- A supervisory attorney must make reasonable efforts to ensure that subordinate attorneys comply with the reporting rules.
- Subordinate attorneys are deemed to have satisfied their reporting obligations once a report is made to a supervisory attorney.
- A subordinate attorney who has reported evidence of a material violation to a supervisory attorney and who reasonably believes that the supervisory attorney has failed to comply with the reporting requirements is permitted, but not obligated, to report the evidence "up the ladder."
- "Appropriate response" means a response that provides a basis for an attorney to reasonably believe that either: (1) there is no occurring material violation, (2) the company has adopted appropriate remedial measures; or (3) the company's board (or other independent committee or a QLCC), has consented to retaining or directing an attorney to review the reported evidence of a material violation and has either implemented the attorney's remedial recommendations or been advised by the attorney that the company or individual can assert a colorable defense in any proceeding relating to the reported violation.
- The final rules have eliminated the documentation requirements contained in the proposed rules with respect to:

  (1) the subordinate's report and

  (2) the basis for the conclusion if the supervisory attorney believes that the information reported by the subordinate attorney need not be reported "up the ladder."

V. The Qualified Legal Compliance Committee (QLCC) Option

The QLCC is a vision initially created by the SEC for regulating attorney conduct in its final rules, codified in 17 CFR Part 205 pursuant to Section 307 of the Sarbanes-Oxley Act. The primary purpose of a QLCC, or optional "independent" board committee, is to provide legal problem oversight for the board on behalf of the corporation. Since the SEC in Part 205 does not require corporations to create a QLCC, it is wise to examine certain aspects of the entity, such as: (i) its function, (ii) its basic structure, (iii) its responsibility and authority, and (iv)its advantages and disadvantages.

A. Function

Section 205.3 (c) of the SEC Final Rules offers the creation of a QLCC as an alternative method of reporting up the ladder. For instance, rather than reporting to a supervisory attorney, company CEO or CLO or Board of Directors, an attorney who discovers evidence of a violation can report directly to a Qualified Legal Compliance Committee (QLCC). The SEC requires that a QLCC be established prior to the event upon which an allegation is based. Specifically, Section 205.3 (c) provides:

> (1) If an attorney… becomes aware of evidence of a material violation… the attorney may, as an alternative to the reporting requirements of paragraph (b) of this section, report such evidence to a qualified legal compliance committee, if the issuer has previously formed such a committee. An attorney who [so] reports… has satisfied his or her obligation to report… and is not required to asses the issuer's response…
>
> (2) A chief legal officer… may refer a report of evidence of a material violation to a previously established qualified legal compliance committee in lieu of causing an inquiry… The chief legal officer (or the equivalent thereof) shall inform the reporting attorney that the report has been referred…

Thus, as an alternative to the prescribed methods of reporting up the ladder, an attorney may seek to disclose evidence of a violation directly to the QLCC—if the corporation has established one—and relieve himself or herself of further reporting responsibilities required by the SEC rules. In doing so, the QLCC allows an attorney to bypass several steps of reporting up the ladder by reporting to a single entity. Similarly, a chief legal officer may refer a report of evidence of a material violation to the company's QLCC, rather than causing an inquiry, and inform the reporting attorney of this course.[58] This reporting approach allows lawyers who discover a potential violation to shift the responsibility of follow-up to the board. The QLCC then assumes responsibility for the investigation, remedial action, or any necessary reporting out required by law. Further, the establishment of a QLCC is encouraged by the Commission in the final SEC rules, because such a structure institutionalizes the practice of assessing evidence of a material violation and promotes a more preventative approach.

B. Basic Structure of a QLCC

Section 205.2(k)(1) defines the structure of a "qualified legal compliance committee of a company." Specifically, it requires a QLCC to have both of the following:

- At least one member of the issuer's audit committee (or, if the issuer has no audit committee, one member from an equivalent committee of independent directors); and
- Two or more members of the corporation's full board of directors who are not employed either directly or indirectly by the company and are not "interested persons" (in the case of a registered investment company) as defined in Section 2(a)(19) of the Investment Company Act of 1940.

C. Responsibilities and Powers

Sections 205.2(k)(2), (3) & (4) provide that a qualified legal compliance committee of a corporation is vested with certain obligations and authority. Specifically, the regulations require that the QLCC:

- Has adopted written procedures for the confidential receipt, retention, and consideration of any report…[59]
- Has been duly established… with the authority and responsibility:

  (i) To inform the issuer's chief legal officer and chief executive officer… of any report of evidence of a material violation (except in the circumstances described in Section 205.3(b)(4));

  (ii) To determine whether an investigation is necessary… and, if it determines an investigation is necessary or appropriate, to:

  (A) Notify the audit committee or full board of directors,

  (B) Initiate an investigation… and

  (C) Retain such additional expert personnel as the committee deems necessary; and

(iii) At the conclusion of any such investigation, to:

(A) Recommend, by majority vote, that the issuer implement an appropriate response… and

(B) Inform the chief legal officer and the chief executive officer…and the board… of the results of any such investigation…;[60] and

- Has the authority and responsibility, acting by majority vote, to take all other appropriate action, including the authority to notify the Commission in the event that the issuer fails in any material respect to implement an appropriate response… [61]

It is important to clarify a few aspects of the QLCC's requisite powers and obligations. First, while QLCC has the authority and responsibility to recommend that an issuer take appropriate remedial action in response to the QLCC's noted violation, it has no authority to direct the issuer to take such action. The reason that the SEC fashioned the rules this way is because vesting QLCC with power to compel the board to act would conflict with established corporate governance models.[62] Any decisions and actions of the QLCC must be made by majority vote, although unanimity is not required. Further, if the corporation materially fails to implement an appropriate response that the QLCC has recommended, the QLCC has authority and responsibility, by way of majority vote, to notify the Commission of such failure.[63]

For guidelines on the mechanics of reporting to a QLCC and sample company procedures, see:

- Securities and Exchange Commission Final Rule: Implementation of Standards of Professional Conduct for Attorneys, 17 C.F.R. pt. 205, 205.2 (k) (2002), available at: http://www.sec.gov/rules/final/33-8185.htm
- General Motors Corporation Qualified Legal Compliance Committee Procedures, at: http://www.acca.com/protected/forms/corpresp/gm_qlcc.pdf
- Joseph T. McLaughlin, Guy N. Molinari, Karen Crupi-Fitzgerald, and Holly Kulka, Qualified Legal, Compliance Committee: Policies and Procedures, Heller Ehrman (April 2003), at: http://www.acca.com/protected/program/qlcc_presentation.pdf

D. Liability of QLCC Members

While neither Section 307 of the Act nor the Final Rules contain any provision regarding the liability of directors who serve on the QLCC, the Commission expressly states in the Final Release that it "does not intend service on a QLCC to increase the liability of any member of a board of directors under state law, and indeed, expressly finds that it would be inconsistent with public interest for a court to so conclude."[64]

E. Issues Presented

(1) QLCC and the Reporting Out Requirement

Some practitioners have commented that the language in section 205.2(k)(4) is ambiguous. While this section states that the QLCC is vested with "authority and responsibility… to take… appropriate action, including the authority to notify the Commission…" it remains unclear whether the QLCC also has the affirmative responsibility to notify the Commission. The fact that the word "authority" refers to the act of notifying the Commission suggests that it may be a permissive— rather than mandatory—code of conduct.

What is also unclear is whether the QLCC would be subject to disciplinary action in the event that it should fail to act properly. Since Congress directed the SEC to establish standards of conduct for lawyers, it is unclear if the SEC may sanction directors under such a directive. Thus, in the spirit of the law, it remains uncertain if the definition of a QLCC provided in section 205.2. (k)(4) should be interpreted to require reporting out, or whether reporting out is merely an option. [65] For more information on this topic, see:

- Susan Hackett, QLCCs: The In-House Perspective, Wall Street Lawyer (May 2004) at: http://www.realcorporatelawyer.com/wsl/wsl0504.html
- Simon M. Lorne, An Issue-Annotated Version of the Sox: A Work in Progress, Munger, Tolles & Olson LLP (December 2003), at: http://www.acca.com/protected/article/corpresp/sarbox_attyethics.pdf

(2) Advantages and Disadvantages of Creating a QLCC

One way to preserve the corporation's ability to use the attorney-client privilege and work product doctrine to protect any information discovered through the course of an investigation is to use a QLCC. A QLCC may retain outside counsel at the outset of an investigation to examine the potential of a material violation. In following this course of action, a QLCC can help prevent increased liability due to disclosure of potentially damaging information.[66]

Curiously, although many corporations quickly adopted the many corporate governance suggestions and mandates, very few have chosen to create a QLCC. One reason is context. While the SEC suggested the creation of the QLCC in its final rules, it drafted the suggestion when mandatory reporting out requirements were still in the rules. Since the reporting out requirements were removed from the final

rule, Part 205, there is little need for a QLCC.[67]

Another reason for the scarcity of these entities is that the creation of a QLCC primarily benefits lawyers, while leaving their director counterparts subject to liability. Corporate boards may be reluctant to establish yet another committee of the Board charged with governance responsibilities, while the entire in-house legal department evades the investigation, assessment and internal reporting responsibilities. Such resistance is a natural response from directors, particularly in light of recent corporate debacles in which director liability has substantially increased. Thus, many in-house lawyers are re-thinking the QLCC suggestion.

Another issue that has hindered the use of the QLCC is the cost in recruiting qualified Directors.[68] Because QLCC members face increased workloads and liability, individuals will often be either reluctant to serve or cost the company too much by demanding the company buy stronger (i.e., costlier) D&O coverage and pay them higher fees than the other directors.

Further, a QLCC can bread animosity amongst the board itself. A board committee that operates apart from—and is more knowledgeable than—management is not compatible with normal corporate functioning. Management, especially the CEO, is therefore apt to resist formation of the QLCC and to refuse to cooperate with it.

After first glance, the structure of the QLCC is suspect.[69] The reason in-house lawyers would promote the establishment of a QLCC is to shift responsibility and liability to an independent committee. However, in order for this to work, the QLCC must hire an independent counsel, unfamiliar with the client's operations. Clearly, a Corporate Legal Officer would not favor this route, as the board committee would be retaining a law firm which is unfamiliar with the corporation to pursue a probing and sensitive investigation, free of any oversight by the corporation's in-house lawyers.

In addition, given the outside firm's lack of experience with the corporation, the costs may be considerably high, and may significantly impact in-house counsel budget. The fact that this may have a negative affect on intra-corporate communications—namely between in-house counsels and corporate directors and executives—makes the QLCC approach appear counter-intuitive from the standpoint of best practices in corporate responsibility. The alternative would be to select in-house lawyers to work with an independent counsel retained by the QLCC. Given this scenario, however, in-house lawyers are subject to liability and increased responsibility, and the QLCC's purpose is largely diminished.

Further, most in-house counsel have a sense of professional obligation and competency in the area of corporate governance. Given that most members of a QLCC are experts in the fields of business and finance, it would seem impractical that they have the time, expertise or interest in making informed decisions regarding

allegations and reports. Although the CLO plays a crucial role in advising the directors in the day-to-day business decisions, the QLCC effectively locks the CLO out of the advising loop. Thus, shifting responsibility to the QLCC raises critical issues as to basic competency of the corporate officers.[70]

However, there are several good reasons in favor of the creation of a QLCC. Referral of a possible material violation to the QLCC should remove any suspicion that the matter would not be dealt with appropriately by management. When a CLO refers a report of misconduct to the QLCC, the CLO is not then required to make any further response to the reporting attorney, other than informing the attorney of the referral. An attorney reporting to a QLCC has no duty to evaluate its response, as otherwise required under the rule. In addition, creating a QLCC may become standard "best practice" in corporate governance. And, although not mandatory, its absence may raise questions about other governance issues.

The continued development of SEC rules and regulations based on the Sarbanes-Oxley Act means that in-house counsel must remain current on legal developments. Counsel should conduct frequent research, or attend legal education classes to ensure awareness of regulations is as current as possible.[71]

For additional dialogue on issues regarding the QLCC option, confidentiality issues, and advantages and disadvantages, the following sources may be useful:

- Susan Hackett, Issues for Law Departments Considering Whether to Recommend that Their Board Create a QLCC, ACCA Memo (August 27, 2003) at: http://www.acca.com/protected/article/corpresp/qlcc_issues.pdf
- Simon M. Lorne, An Issue-Annotated Version of the Sox: A Work in Progress, Munger, Tolles & Olson LLP (December 2003), at: http://www.acca.com/protected/article/corpresp/sarbox_attyethics.pdf
- Joseph T. McLaughlin, Guy N. Molinari, Karen M. Crupi-Fitzgerald, and Holly Kulka, Qualified Legal Compliance Committee: Policies and Procedures, Heller Ehrman White & McAuliffe LLP, at 13-16 (April 2003), available at: http://www.acca.com/protected/program/qlcc_presentation.pdf
- Memo Regarding What Legal Departments Can Do to Prepare for Compliance with New SEC Rules, ACCA Memo, at 1-2, available at: http://www.acca.com/protected/article/corpresp/8krule.pdf
- The New Sarbanes-Oxley Attorney Responsibility Standards, ACCA Docket 21 no. 5 (May 2003), available at: http://www.acca.com/protected/pubs/docket/mj03/standard2.php
- Paul S. Maco, Kevin Lewis and David Godschalk, The Qualified Legal Compliance Committee: A Practical Choice?, Securities Regulatory Update (June 9,

2003).

- Audrey Strauss, Qualified Legal Compliance Committees: Pros and Cons, New York Law Journal (May 1, 2003).
- Susan Hackett, QLCCs: The In-House Perspective, Wallstreetlawyer.com: Securities in the Electronic Age (May 2004).

VI. Drafting a Company Policy

Many corporate legal departments have responded to the new rules by drafting policy statements and guidelines to aid attorneys with proper professional conduct. Some companies with pre-existing professional guidelines will simply reiterate the comprehensive policies already in place, while others will develop new guidelines. Whatever the case, it is important to bear in mind a few key issues in forming a sample policy for your company.

First, identify the various purposes for drafting a policy. These may include:

- Attorney Interest: Rules of professional responsibility regulating attorney conduct.
- Client Service/Liability Interests of Law Department: Mandate proper management policies that ensure reports are made and remedies are sought in response to allegations.

Drafting a policy with these distinct goals in mind will best enable your legal department to balance the obligations imposed by the Commission's rules and company policies with their duty to act in the best interest of their clients. This approach can dispel the notion that attorneys are now in the "gotcha!" reporting business, and recognize instead that counsel are members of a corporate team, responsible for legal counseling and preventive compliance.[72]

- **Sample Policies:** Developing a policy is necessary, but not sufficient. It is essential to educate employees about what the policy means, when to ask questions, whom to turn to for aid, and the importance of ethical conduct to the company. To view the comprehensive plans of companies such as BellSouth Corporation, Duke Energy Corporation, General Electric Company, General Motors Corporation, Hasbro, Inc., PepsiCo, Inc., Starbucks, Xerox Corporation, check out the following:

  Emerging and Leading Practices in Sarbanes 307 Up-The-Ladder Reporting and Attorney Professional Conduct Programs: What Companies and Law Firms are Doing, Leading Practice Profiles Series, ACC (September 4, 2003), at: http://www.acca.com/protected/article/corpresp/lead_sarbox.pdf

  Guidelines Regarding SEC Standards of Professional Conduct for Attorneys, Palmer and Dodge LLP, at: http://www.acca.com/protected/policy/conduct/palmerdodge.pdf

  Law Department Polices/Memoranda, Hasbro, Inc. Mission Statement, at: http://www.acca.com/protected/policy/conduct/hasbro.giv

  Leading Practices in Codes of Business Conduct and Ethics: What Companies are Doing, Best Practices Profiles Series, ACCA (August 2003), at: http://www.acca.com/protected/article/ethics/lead_ethics.pdf

  Office of General Counsel Policy Compliance with SEC Attorney Conduct Standards, Policy Statement, Xerox Corporation (August 1, 2003), at: http://www.acca.com/protected/policy/conduct/xerox.pdf

  Memo to In-House Attorneys re: SEC Standards, General Motors, at: http://www.acca.com/protected/policy/conduct/gm_inhouse.pdf

- **Tips**

  Five Practical Steps for In-house Counsel Concerned about Changes in Lawyer Regulation Pursuant to Sarbanes-Oxley Section 307, available at: http://www.acca.com/legres/corpresponsibility/307/steps.pdf

  Broc Romanek and Kenneth B.Winer, Practical Tips for Dealing with the New Attorney Responsibility Standards, ACC Docket 21 no. 5 (May 2003): 40-55, available at: http://www.acca.com/protected/pubs/docket/mj03/standard_tips.php

VII. Whistleblowers

A. Protection for Whistleblowers

Sarbanes-Oxley creates a new claim for employees, including attorneys, fired or treated adversely because of a complaint or report of conduct by a company that violates Sarbanes-Oxley.[73] If an attorney who was formerly employed or retained by an issuer who has reported evidence of a material violation reasonably believes that he or she has been discharged on the basis of his or her report, such attorney may notify the board of directors of such discharge. In-house attorneys may fur-

ther avail themselves of the benefit of Section 806 of Sarbanes-Oxley Act, which offers whistleblower protection. However, given the traditional limitations on wrongful discharge, and respecting a client's fundamental right to choose counsel, it remains to be seen if this provision will be of significant value to in-house counsel who shed light upon corporate misfeasance.

Section 806 of Sarbanes-Oxley, entitled "Whistleblower Protection for Employees of Publicly Traded Companies," strictly prohibits companies from engaging in retaliation against an employee for (1) providing information or making a complaint regarding conduct the employee "reasonably believes" constitutes a securities violation or securities fraud, or (2) filing or participating in proceedings related to fraud against shareholders. Employers (and in some cases individuals) found to have retaliated against a whistleblower may be subject to administrative, civil, and criminal sanctions. The whistle-blowing protections of the Act apply not only to publicly-traded companies, but also to their officers, employees, contractors, subcontractors, and agents. The Act specifically protects employees, including counsel, when they take lawful acts to disclose information or otherwise assist criminal investigators, federal regulators, Congress, supervisors (or other proper people within a corporation), or parties in a judicial proceeding in detecting and stopping fraud. All that the Act requires is that the employee reasonably believes that a violation of federal securities law, the rules of the SEC, or "any provision of Federal law relating to fraud against shareholders" has occurred or is occurring. The Act protects employees who complain to any person at the company with the authority to "investigate, discover, or terminate misconduct," which likely includes all corporate counsel and human resources professionals. This statutory language would appear to allow for individual liability of officers and employees. If the employer takes illegal action in retaliation for lawful and protected conduct, the Act allows the employee to file a complaint with the Department of Labor ("DOL").

Sarbanes-Oxley protects two broad classes of conduct. First, an employee is protected from retaliation when providing information, causing information to be provided, or otherwise assisting in the investigation of conduct that "the employee reasonably believes" constitutes wire fraud, bank fraud, securities fraud, or violation of "any rule or regulation of the Securities and Exchange Commission, or any provision of Federal law relating to fraud against shareholders." Second, the Act protects an employee from retaliation for filing, causing to be filed, testifying in, participating in, or otherwise assisting in a proceeding filed or about to be filed (that the employer knows about) relating to the types of fraud listed above.

The "whistleblower" employee must file a complaint with DOL within 90 days of the alleged retaliation. The whistleblower's initial burden of proof is to show that the protected activity (i.e., complaint relating to fraud against the shareholders) was "a contributing factor" in the adverse employment decision. By contrast, the employer must prove "by clear and convincing evidence" that it would have taken

the same adverse employment action even in the absence of the whistleblower's protected activity. If DOL decides to hold a hearing, it must do so expeditiously and must issue a final order within 120 days of the hearing. The employee can bring the matter to federal district court only if DOL does not resolve the matter within 180 days (and there is no showing that such delay is due to the bad faith of the claimant) as a normal case in law or equity, with no amount in controversy requirement. The Act provides for reinstatement of the whistleblower, back pay with interest, and compensatory damages to make the whistleblower whole, including reasonable attorneys' fees and costs, as remedies if the whistleblower prevails. The Act does not provide for either punitive damages or a jury trial. Judicial review is only available through an appeal to the Court of Appeals, but such appeal does not automatically stay the Department of Labor's order.

The Sarbanes-Oxley Act also makes it a felony offense for any person to "knowingly" and "with the intent to retaliate" take "any action harmful" to a person for providing truthful information to a law enforcement officer relating to the commission or possible commission of "any Federal offense."[74] The statute makes it clear that "harmful" conduct includes interference with employment but it does not define what additional harm may violate the law. This provision is noteworthy because it protects a broader class of whistleblowers than do the civil provisions of Sarbanes-Oxley. The statute protects truthful reporting of information relating to any federal offense, not just information relating to securities or other corporate fraud. Violation of this provision is punishable by fines of up to $250,000 for individuals and $500,000 for companies, ten years' imprisonment, or both.

On February 15th, 2005 Administrative Law Judge Stephen Purcell ordered Cardinal Bankshares Inc. to reinstate its former chief financial officer, David Welch, and pay him nearly $65,000 in back pay and damages.[75] The significance is that Welch became the first person to win protection as a whistleblower under the Sarbanes-Oxley Act, passed by Congress in 2002 in the wake of corporate scandals at Enron, WorldCom and other firms.

Since the law took effect in mid-2002, about 750 people have filed complaints with the Department of Labor, alleging that their employers retaliated against them for calling attention to financial mismanagement. The Labor Department oversees such cases in a three-step process that an employee must exhaust before going to federal court. The number of cases has risen with about 150 in the law's first year and nearly twice that in its third.[76] Welch is one of just three workers to win protection so far. Fewer than 100 cases have ended in settlements.[77] While the case will be appealed in federal court, it suggests that the Whistle-blower provisions of Sarbanes will be enforced by the courts.

For legislative materials, see:

- Securities and Exchange Commission Final Rule: Implementation of Standards of Professional Conduct for Attorneys, 17 C.F.R. pt. 205 (2002), available at: http://www.sec.gov/rules/final/33-8185.htm

- Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745, Section 307 (2002), available at: http://www.acca.com/legres/enron/sarbanesoxley.pdf

B. Whistle-blowing/Noisy Withdrawal

A pertinent question is will an attorney face any culpability if, after having reported the matter all the way 'up the ladder'—from his supervising attorney to the CLO, CEO and directors—the attorney learns that no action was taken?

In response to practitioner comments, state ethics regulators and foreign lawyers, the SEC deferred and/or eliminated some of the most controversial provisions that many believe were beyond the spirit of Sarbanes-Oxley. Initially, the SEC required that any attorney dissatisfied with the client's response must make "a noisy withdrawal."[78] Under the SEC's alternative rule, however, the corporation, rather than the reporting attorney, is required to notify the SEC regarding the circumstances of withdrawal. The following chart compares the requirements under the initial proposal with those contained in the proposed alternative rule.[79] Also note that the proposed alternative requires the corporation to file a form 8-K.

	Originally Proposed Rules	Alternative Rule
Circumstance	Reporting attorney who has not received an appropriate response in a reasonable time	Reporting attorney who has not received an appropriate response in a reasonable time
Standard	Reporting attorney believes the material violation is either ongoing or is about to occur and is likely to result in substantial injury to the company or investors	There is substantial evidence that a material violation is ongoing or about to occur
Attorney Requirement "withdrawal" Reporting Firm Attorney:	Under these circumstances, attorney must withdraw from representation.	Under such narrow circumstances, reporting attorney MUST: • Withdraw from representation; • Immediately cease to engage in any matter regarding the alleged violation; and • Firm Attorney: Notify the company in writing that the company has not provided an appropriate response in a reasonable time
Reporting In-house Counsel "withdrawal"	In House Counsel: may, but is not required to withdraw from representation.	In-house Counsel: Notify the board stating that he or she will not be allowed to continue to work for the client on related issues for professional reasons, but does not need to resign.
SEC Notification "noisy"	Reporting attorney MUST notify the SEC within one business day that the withdrawal was based on business considerations AND disaffirm any false or materially misleading submissions to the SEC that s/he has helped prepare.	Reporting attorney NOT required to notify the SEC of the withdrawal, but is permitted to do so if the company did not report the attorney's notice.
Company Requirement		Company must, upon receiving such written notice from reporting attorney, report such notice and related circumstances on Form 8-k, 20-F or 40-F, within two business days of receipt.

In a speech to the ABA Business Law Section on April 3, 2004, SEC General Counsel Giovanni Prezioso said that although the Commission has not yet decided whether to proceed with a mandatory "noisy withdrawal" rule, it is closely monitoring attorney compliance with the new "up the ladder" rule as well as the bar's efforts to address the concerns raised by Congress in enacting Section 307.[80] It would appear that so long as Model Rules 1.13 and 1.6 are effective, they SEC will not attempt to enact regulations mandating a "noisy withdrawal."

For list format of noisy withdrawal alternatives, see:

- Attorney-Client Privilege in the Corporate Setting Fact Sheet, at 25, Quinn

Emanuel Urquhart Oliver & Hedges, LLP, at: http://www.acca.com/chapters/socal/program/corpattyclient.pdf

For recommendations on noisy withdrawal alternatives, see:

- Barry Nagler and M. Elizabeth Wall, ACC's Second Comment Recommendations on Noisy Withdrawal, File No. S7-45-03 (April 7, 2003), available at: www.acca.com/advocacy/307comments2.pdf.

For information on the SEC rules on the new attorney standards and its alternative proposal of creating a Form 8-K public reporting requirement by the board, see:

- Stanley Keller, SEC Implements Standards of Professional Conduct for Attorneys, ACC and Palmer & Dodge LLP, available at: http://www.acca.com/legres/corpresponsibility/307/summary.pdf

Critics comment that any permissive withdrawal should allow a reporting attorney to withdraw from representing its client on the matter at issue, but continue representation otherwise. For a discussion, see:

- Robert S. Risoleo, Sullivan & Cromwell Memoranda, Advanced Doing Deals 2003: Dealmaking in the New Transactional Marketplace, Practicing Law Institute (June 19-20, 2003), 1377 PLI/Corp 529, Order No. B0-01UN.

C. Preventative Measures

There are several steps that GCs can take to protect themselves and their companies from the threat of criminal and civil sanctions under the Sarbanes-Oxley whistleblower provisions:81

- **Impress upon your company the importance of establishing an effective internal compliance program.** Such a program should include clear policies regarding corporate ethics and conduct, internal reporting procedures, and training of employees and executives regarding these rules and their responsibilities and potential liability.

- **Adopt or revise codes of conduct.** The code should reflect both the culture of the company and the standards of conduct expected from the company. The code should also encourage employees to report potential financial, ethical, legal, or other misconduct.

- **Examine job descriptions.** Manager and supervisory job descriptions should reflect their duties and responsibilities with regard to corporate compliance. This communicates to managers and supervisors that the company takes compliance seriously and that it prohibits retaliation for reporting suspected misconduct.

- **Establish response and investigation procedures.** Written procedures should be in place for documenting and responding to employee complaints regarding alleged corporate fraud.

- **Train and educate employees regarding corporate compliance.** Communicate to non-supervisory employees about the company's expectations regarding accurate reporting of company financial information and reporting potential misconduct. The company should also make it clear that employees who report alleged misconduct in good faith will not be subjected to discrimination, harassment, or retaliation.

- **Properly document discipline and termination.** Because the close timing of an employee's termination relative to a complaint made by that employee regarding corporate compliance may create the appearance of retaliation, it is critical to carefully document employee performance problems as they come up and at termination. Managers and supervisors should carefully document employee performance deficiencies, and these records should be maintained.

VIII. Attorney-Client Privilege Issues

A. Confidentiality & Model Rule 1.6

The issue of confidentiality in the representation of the corporation as a client is complex, especially since the corporation can only act through its agents—namely corporate executives and board members. The recent changes in the SEC Rules regarding attorney confidences further complicate matters. The purpose of the revised ABA Rule is to help "prevent a client from using a lawyer's services to commit a crime or fraud that results in substantial financial injury to innocent third parties."82

The ABA modified Rule 1.6 of the Model Rules on Professional Responsibility to allow attorneys to report evidence of a client corporation's ongoing or future financial fraud if and only if the fraud is reasonably likely to have a significant financial impact on third parties and if the lawyer's services have been used by the client in the commission of such a fraud.[83] However, state regulations differ on how attorneys should respond in this situation. As states may impose more rigorous attorney standards, the SEC does not preempt this field entirely; however, it certainly prevails where there is a conflict. In particular, such a conflict will exist in states that do not allow attorneys to break client confidences to prevent financial harm or fraud.

The SEC Rules permit an attorney to reveal confidences to the Commission, with-

out the issuer's consent, under the following circumstances:

- to prevent the company from committing a material violation that is likely to cause substantial injury to the financial interests of that company or its investors,
- to prevent the issuer from committing perjury during a Commission or administrative investigation, or
- to rectify the consequences of a material violation by the issuer that has caused, or may cause, substantial injury to the financial interests of the company or its investors.

Thus, a lawyer may disclose to the Commission certain civil violations not rising to level of a crime, if such violations have been reported "up the ladder" and a response has been inadequate. Although this may conflict with a state rule that may require such reporting, the SEC has stated that the SEC rules would prevail in such instances.[84] In effect, this position would entail federalizing the SEC rules on ethics. Further, under the SEC Rule 205.6(c), a lawyer may not be liable for complying with the SEC Rules in good faith, even if such an action would be inconsistent with the standard of conduct dictated by state rules. Meanwhile, several states question whether Congress intended to extend power to the SEC to allow a breach of attorney-client privilege in states, such as Washington and California, which do not authorize such a breach of confidences.

B. Reporting Up the Ladder: SEC Regulations and Model Rule 1.13

The SEC Rules contain another important provision relating to confidentiality: Rule 205.3(d)(2) allows an attorney to reveal confidential information related to the attorney's representation if they reasonably believe such revelations are necessary to:

(1) prevent a material violation that will injure the company or stockholders

(2) prevent perjury,

(3) to rectify the consequences of a material violation.

In the same manner, Model Rule 1.13 allows attorneys to reveal information to prevent a violation that is reasonably certain to result in substantial injury to the organization and most likely shareholders. Model Rule 1.13 requires corporate attorneys to report law violations by officers and employees up-the-ladder within the organization and, if necessary, to report corporate violations outside the organization. The Model Rule provides that if a lawyer representing a corporation knows

that a corporate officer / corporate employee is engaged in a violation of law that is likely to result in "substantial injury to the organization", the lawyer must proceed in a manner that is in the best interest of the organization.[85]

Unless the lawyer reasonably believes that it is not necessary to do so, they must also refer the matter to a higher authority in the organization that can act on behalf of the organization. I the up-the-ladder provisions of Model Rule 1.13(b) fail, the Model Rules, allow the lawyer to reveal information relating to the representation, whether or not Model Rule 1.6 might prevent such disclosure.[86] This provision specifically allows lawyers to reveal confidential client information outside the organization.

Both of these provisions, the SEC rule and the ABA Model Rule, override Model Rule 1.6 and its state counterparts, which in some will prevent the revelation of information.

The SEC Rule augments and provides greater clarity than the ABA Model Rule. It specifies when attorneys have the option to report out, without making such reporting mandatory. The rule corresponds to ethics rules adopted by "the vast majority of states," even though it is slightly broader than the Model Rule 1.13.[87]

SEC Rule 205.3(d)(2) is a permissive rule, not a mandatory one. Attorneys may reveal to the Commission information that will help "prevent the issuer from committing a material violation that is likely to cause substantial injury to the financial interest of property of the issuer or investors."[88] This corresponds closely with Model Rule 1.13, which states that a lawyer may reveal information "if the lawyer reasonably believes that the violation is reasonably certain to result in substantial injury to the organization."[89]

C. Impact on Attorney-Client Relations

The role of the attorney is not only to defend clients after a crime has been committed, but to prevent their commission through effective communication with the client regarding the specific aspects of applicable laws. The sheer complexity of Sarbanes-Oxley and related state securities laws will help ensure that clients will continue to seek out legal advice, regardless of the new reporting requirements. In the post-Enron world lawyers will need to be constantly on the lookout for client misconduct, or the perception that there is misconduct, if they hope to effectively protect the company and ultimately, themselves.

The SEC Rule and the Model Rule may likely serve to strengthen the relationship between attorneys and their true clients: corporations. Model Rule 1.13 provides that a corporation is the client to whom duties of confidentiality are owed, not the organization's directors, officers, or employees.[90] An attorney is justified, and reasonably obligated, to inform the client (the company) that it's agent are acting

in a detrimental manner.

In the end, it is likely that clients (the individuals who represent the company) do not rely on confidentiality rules as much as lawyers believe. Limiting the privilege will probably not change revelations of clients' confidences or affect their relationship with in-house counsel.

Model Rule 1.13 implies that in-house counsel and corporate attorneys must reevaluate their roles in corporations. Before Enron, Worldcom, etc. corporate law viewed in-house lawyer as advocates whose duty was zealous representation of clients, including corporate directors and officers.[91] The passage of Model Rule 1.13 imposes upon counsel new responsibilities. Model Rule 1.13 reminds corporate lawyers of individual responsibility to maintain their professional role and to not cross over from their position of company advocate to partner to a client. These new limitations on the applicability of the in house lawyer's role as an advocate may help lead to better corporate compliance.

For discussion on preemption issues, see:

- Stanley Keller, SEC Implements Standards of Professional Conduct for Attorneys, ACC and Palmer & Dodge LLP, available at: http://www.acca.com/legres/corpresponsibility/307/summary.pdf
- Chi Soo Kim and Elizabeth Laffittee, The Potential Effects of SEC Regulation of Attorney Conduct Under the Sarbanes-Oxley Act, 16 Geojle 707 (2003) (discussing preemption issues).
- Mathew S. Rosengart, Protecting the Corporation and Yourself After Enron and Sarbanses-Oxley: A Primer for Lawyers Practicing Before the SEC and DOJ, 2003 The Federal Lawyer 34.
- Washington State Bar Interim Ethics Opin. (July 26, 2003), (challenging SEC's position on preemption) available at: www.wsba.org/lawyers/groups/ethics2003/formalopinion.doc

IX. Privately Held Companies and Non-Profits

Although the impetus for drafting model rules and policies is to regulate lawyers at public companies, many private companies are looking at adopting similar guidelines. This is attributed in large part, to the emerging perspective among state legislatures, state bars, and stakeholders that lawyers representing all companies,

public and private, should be concerned about corporate responsibility.

It is worth noting that public and private companies alike have to adhere to whistleblower provision under Sarbanes-Oxley, under which employees must be permitted to anonymously notify regulators of any potential wrongdoing within a company. As Chief Justice Veasey of Delaware's, Supreme Court stated:

> "I do think the changes in corporate governance that we're seeing through the voluntary best practices codes, for example… have created a new set of expectations for directors. And that is changing how courts look at these issues."[92]

In addition, privately held companies must take many of the steps required to demonstrate compliance with Sarbanes-Oxley if they decided to go public or agreed to merge with a public company. Both issues illustrate the current impact SOX can have on any private company operating in today's marketplace.

A study by Foley & Lardner LLP found that private companies and nonprofit organizations are embracing many of the reforms imposed on public companies by the Sarbanes-Oxley Act. The study found that "87 percent of private firms and nonprofits said the reforms mandated by Sarbanes-Oxley are having an impact on their operations, up from 77 percent in 2004."[93] Examples of the impact include:

- 75 percent of those surveyed now require board approval of non-audit services provided by the organization's auditor
- Almost 68 percent also said they require their CEO and CFO to certify financial results
- 72 percent said they had put protections in place for whistle-blowers[94]

Additionally, the study found that nonprofits are more amenable than private companies to restricting executive compensation, with 59 percent of nonprofit respondents saying they planned to implement such restrictions, compared to only 38 percent of for-profit companies.[95]

Sarbanes-Oxley, and the related regulations by the SEC and PCAOB, has significantly the legal practice in many areas of corporate governance and financial compliance for public companies. As states and the federal government continue to evaluate the effects of Sarbanes-Oxley, private and non-profit companies should expect that several of these requirements will be extended to them. In one example, California passed the nations first governance law for nonprofits, which, in part requires charities that do business in the state and have revenues exceeding $2 million to form audit and compensation committees.[96] In 2005, at least 8 states (including New York, New Jersey, and Arkansas) have also considered extending provisions of Sarbanes-Oxley into the non-profit sector.

By taking action now to comply voluntarily with as many of these requirements is reasonable, larger private companies (or those companies which desire to go public or being acquired) can ease their transition into the public sector or the future of corporate regulation. At the same time, these companies can reduce their litigation exposure.

To view best practices of corporate governance policies of privately held companies and non-profit organizations, as well as discussion on why private company lawyers should be concerned about Sarbanes-Oxley, see:

- Leading Practices in Codes of Business Conduct and Ethics: What Companies are Doing, Best Practices Profiles Series, ACC (August 2003), at: http://www.acca.com/protected/article/ethics/lead_ethics.pdf
- Hot Topics in Representing Nonprofits, ACCA's 2003 Annual Meeting, Course Materials (November 2003), available at: http://www.acca.com/education03/am/cm/509.pdf
- Susan Hackett, It's Private Companies' Turn to Dance the Sarbox Shuffle, ACCA Paper (August 2003), available at: www.acca.com/public/article/corpresp/sarbox_shuffle.pdf.
- Harvey Goldschmid, Comm. Speech, Securities and Exchange Commission, Orison S. Marden Lecture, Association of the Bar of the City of New York (November 17, 2003) (discussing non-profits and non-publicly traded companies), available at: http://www.sec.gov/news/speech/spch111703hjg.htm
- Paul Broude, Richard Prebill, Foley & Lardner, LLP, The Impact of Sarbanes-Oxley on Private & Nonprofit Companies, Presentation at the 2005 National Directors Institute (March 10th, 2005), available at: /www.foley.com/files/tbl_s60WorkingGroups/FileUpload627/69/privatestudydraft3-04-05.pdf
- Jeffrey S. Cronn, Sarbanes-Oxley trickles down to nonprofits, The Business Journal – Portland, (April 1, 2005)
- Thomas Hoffman, Direct and indirect impact of Sarbanes-Oxley hits private companies: Companies considering IPOs or mergers must now address accountability issues, Computerworld (July 25th, 2003); available at: computerworld.com/governmenttopics/government/legalissues/story/0,10801,83457,00.html
- Linda Kelso, Voluntarily, private companies get into oversight act, Jacksonville Business Journal (May 6, 2005), available at: jacksonville.bizjournals.com/jacksonville/stories/2005/05/09/focus3.html

X. Document Retention Procedures

A. Introduction to Document Retention

Managing records is an important challenge within a corporation, regardless of its size. This is especially true in light of the Sarbanes-Oxley Act and the related Securities and Exchange Commission's rules on Management's Report in Exchange Act Periodic Reports.[97] The impetus for records management, in addition to compliance with the Sarbanes-Oxley mandates, is to restore investor confidence. Thus, the new rules add additional requirements and consequence components, emphasizing the importance of records.

B. How Does the Sarbanes-Oxley Act Affect Companies' Document Retention Obligations?

The Act, as well as the regulations which were implemented following its passage, imposed new requirements and duties on affected companies. These include:

(1) Criminalization of the Destruction, Alteration and Falsification of Records in Federal Investigations, Bankruptcy Cases and Official Proceedings - Sections 802 and 1102 of the Act amended the federal obstruction of justice statute, Title 18 of the United States Code (Crimes and Criminal Procedure), to significantly increase penalties for the destruction, alteration and falsification of records in certain circumstances.

(2) Section 802 provides for a fine and/or imprisonment up to 20 years for anyone who knowingly "alters, destroys, mutilates, conceals, covers up, falsifies, or makes a false entry" in any record or document with intent to impede, obstruct or influence the investigation or administration of any matter within the jurisdiction of a federal department or agency or any bankruptcy case. 18 U.S.C. § 1519.

(3) Section 1102 establishes the same penalty as Section 802 for anyone who corruptly "alters, destroys, mutilates, or conceals" a record or document with intent to impair its integrity or availability for use in an official proceeding. 18 U.S.C. § 1512(c). Significantly, the official proceeding need not be pending or about to be instituted at the time of the offense. Id. § 1512(f)(1).

(4) New Federal Sentencing Guidelines Related to Obstruction of Justice. Section 805 of the Act commands the Sentencing Commission to review and amend the Sentencing Guidelines to ensure that the base offense level and sentencing enhancements are sufficient to deter and

punish obstruction of justice. The Commission has proposed amendments that would increase the base offense level for obstruction-of-justice offenses by two and create a two-level enhancement for the destruction, alteration or fabrication of records in certain circumstances. 68 Fed. Reg. 2615 (proposed January 17, 2003). If adopted, these changes would increase the penalties for anyone convicted of these offenses.

(5) Broader Record Retention Requirements for Auditors of Public Companies. Section 101(a) of the Act establishes a Public Company Accounting Oversight Board to oversee the audit of public companies, and Section 103(a)(2)(A)(i) commands the Board to adopt auditing standards that require accounting firms to "prepare, and maintain for a period of not less than seven years, audit work papers, and other information related to any audit report, in sufficient detail to support the conclusions reached in such report." In addition, Section 802 of the Act amends Title 18 of the United States Code to require auditors of publicly held companies to maintain "all audit or review workpapers" and directs the SEC to enact related regulations. 18 U.S.C. § 1520(a)(1) and (2). The SEC regulations, which apply to all audits or reviews completed on or after October 31, 2003, establish a seven-year retention period for "records relevant to the audit or review, including workpapers and other documents that form the basis of the audit or review, and memoranda, correspondence, communications, other documents, and records (including electronic records), which (1) are created, sent or received in connection with the audit or review, and (2) contain conclusions, opinions, analyses, or financial data related to the audit or review." 17 C.F.R. § 210.2-06(a). In addition to the audit or review of financial statements of publicly traded companies, the retention requirement applies also to the audit or review of financial statements of registered investment companies. Id. Knowing or willful violation of Section 802 (a)(1) of the Act or the related SEC regulations is punishable by fine and up to 10 years of imprisonment. 18 U.S.C. § 1520(b).

For more guidance on records retention practices in light of Sarbanes-Oxley, see:

- Leading Practices in Information Management and Records Retention Programs: What Companies are Doing, Best Practices Profiles Series, ACC (August 2003), available at: http://www.acca.com/protected/article/records/lead_infomgnt.pdf
- Records Retention Enforced Corporate Records Programs, ACC InfoPAK (December 2003), available at: http://www.acca.com/infopaks/recretent.html
- Document Retention After Sarbanes-Oxley, http://www.perkinscoie.com/content/ren/updates/corp/093003.htm

XI. Sanctions and Other Standards of Professional Conduct

The following points address applicable sanctions that apply to attorneys who fail to comply with Sarbanes-Oxley:[98]

- Violators of the rules are subject to civil penalties and remedies, including administrative disciplinary proceedings that could result in a censure or a suspension or bar from practicing before the SEC.
- Attorneys who comply in good faith with the rules are not subject to discipline under inconsistent state rules.
- Foreign attorneys (who do not qualify as "non-appearing foreign attorneys") are exempt from the rules to the extent their own laws would prohibit compliance.
- The rules do not provide for criminal liability and expressly state that no private right of action is established.
- The rules set forth a minimum standard of professional conduct for attorneys appearing before the SEC; these standards are meant to supplement, but not replace, applicable state standards.
- Where a state standard actually conflicts with the standard in the rules, the rules govern.

The Sarbanes-Oxley Act has also added numerous criminal sanctions to the SEC's enforcement arsenal. These include:

- The Corporate Responsibility Act (Title III)
- The Corporate and Criminal Fraud Accountability Act (Title VIII)
- The White-Collar Crime Penalty Enhancements Act of 2002 (Title IX)
- The Corporate Fraud Accountability Act of 2002 (Title XI).

(1) The Corporate Responsibility Act (Title III)

In §302, "Corporate Responsibility for Financial Reports", the CEO and the CFO are required to prepare a statement to accompany the audit report to certify the

"appropriateness of the financial statements and disclosures contained in the periodic report, and that those financial statements and disclosures fairly present, in all material respects, the operations and financial condition of the issuer."

A violation must be knowing and intentional to give rise to liability. As an example of how this standard may provide accused officers with a defense, one need only look at the HealthSouth lawsuit. Richard M. Scrushy, former chairman and CEO of HealthSouth Corporation, has argued that his financial executives were the ones responsible for his company's $2.5 billion accounting fraud. Scrushy has claimed that he only signed off on fraudulent accounting figures because he "unknowingly" trusted the five CFOs who had served under him. His argument may serve to provide him with a non-guilty verdict.

The criminal fraud provisions of this section make a distinction between a CEO who "knowingly" signs off on inaccurate financial statements and one who does so "willfully and knowingly." "Knowing violations" are punishable by up to 10 years in jail and $1 million in fines, while those individuals who sign inaccurate statements "willfully and knowingly" face 20 years and a $5 million fine.

The Sarbanes-Oxley Act also allows for the redirection of civil penalties paid by violations. Previously, all civil penalties were paid into the U.S. Treasury. Under the §308, "Fair Funds for Investors" provision, the SEC has the authority to direct civil penalties to defrauded investors. Examples of the use of this provision:

- WorldCom, Inc., agreed to satisfy its civil penalty obligation by paying $500 million in cash and $250 million in stock to defrauded investors.
- Merrill Lynch will pay investors $80 million,
- JP Morgan Chase ($135 million), and
- Citigroup ($120 million).

(2) The Corporate and Criminal Fraud Accountability Act (Title VIII)

"Anyone who knowingly alters, destroys, mutilates, conceals, covers up, falsifies, or makes a false entry in any record, document, or tangible object with the intent to impede, obstruct, or influence the investigation or proper administration of any matter within the jurisdiction of any department or agency of the United States can be fined, imprisoned for up to 20 years, or both"[99]

§807 states that anyone who knowingly executes, or attempts to execute, a scheme or artifice to defraud any person in connection with a securities issue or attempts to obtain, by means of false or fraudulent pretenses, representations, promises, money, or property, in connection with the purchase or sale of any security, can be fined, or imprisoned up to 25 years, or both.

(3) The White-Collar Crime Penalty Enhancements Act of 2002 (Title IX)

Individual corporate officers or employees who certify a financial statement (required under §302) knowing that the periodic report accompanying the statement does not comply with this section can be fined up to $1 million, imprisoned up to 10 years, or both. If found to have done so "willfully," the penalty shall be increased to a fine up to $5 million and imprisonment up to 20 years, or both.[100]

(4) The Corporate Fraud Accountability Act of 2002 (Title XI)

§1102 of Title XI can also be used to prosecute corporate officials. Individuals who corruptly alter, destroy, mutilate, or conceal a document with the "intent to impair the object's use in an official proceeding", can be fined, imprisoned up to 20 years, or both. This rule also applies to those who obstruct, influence, or impede any official proceeding, Under §1106 fines rose from up to $1 million / 10 years to $5 million and up to 20 years in prison. The SEC also was provided with the authority to prohibit any person who has violated section 10(b) or the rules or regulations from serving as an officer or director of a registered company. [101]

For additional information regarding attorney sanctions, the following materials may be insightful:

- Attorney-Client Privilege in the Corporate Setting, Fact Sheet, at 27, Quinn Emanuel Urquhart Oliver & Hedges, LLP, available at: http://www.acca.com/chapters/socal/program/corpattyclient.pdf.
- Stanley Keller, SEC Implements Standards of Professional Conduct for Attorneys, ACC and Palmer & Dodge LLP, available at: http://www.acca.com/legres/corpresponsibility/307/summary.pdf

XII. Additional Resources

ACC Resources

Gregory R. Watchman, Sarbanes-Oxley Whistleblowers: Avoiding the Nightmare Scenario, ACC Docket 24, no. 4 (April 2006): 38-55 available at http://www.acca.com/protected/pubs/docket/apr06/watchman.pdf

Green Eye Shades For Lawyers: A Toolkit, ACC Docket 23, no.3 (March 2005): 62-67 http://www.acca.com/protected/pubs/docket/mar05/toolkit.pdf

Danette Wineberg and Philip H. Rudolph, Corporate Responsibility: What Every Lawyer Should Know, ACC Docket 22, no. 5 (May 2004): 68-83 available at http://www.acca.com/protected/pubs/docket/may04/social.pdf

Peter Connor, If The Other Hat Fits- Wear it: A Guide To Effective Business Partnering, ACC Docket, 22, no. 9 (October 2004): 88-102 available at http://www.acca.com/protected/pubs/docket/oct04/partner.pdf

John K. Villa, Investigative Attorneys and the Reporting Obligations Under the SEC's Professional Conduct Rules, ACC Docket 22, no. 4 (April 2004): 133-137 available at http://www.acca.com/protected/pubs/docket/apr04/ethics.pdf

John K. Villa, Ethics & Privilege: Hidden Storms for Those in Safe Harbors: The SEC's Professional Conduct Rules and the Federal Preemption Doctrine, ACC Docket 22, no.2 (February 2004): 81-85 available at http://www.acca.com/protected/pubs/docket/feb04/ethics.pdf

Broc Romanek and Kenneth Winer, The New Sarbanes-Oxley Responsibility Standards, ACCA Docket 21, no. 5 (May 2003): 40-55, available at: http://www.acca.com/protected/pubs/docket/mj03/standard1.php

Richard F. Ober Jr. and Michael Parish, Maybe You Need a Lawyer: Does the Sarbanes-Oxley Act Make the SEC Your Client? ACC Docket 21, no. 4 (April 2003): 70-85, available at: http://www.acca.com/protected/pubs/docket/am03/client2.php

Joanne L. Bober, J. Alberto Gonzalez-Pita, et al. Closing Program: When "Jeopardy" Is No Longer a Game Show: Safeguarding Against Personal, Professional, & Fiduciary Liability, 2004 ACC Annual Meeting presentation, available at http://www.acca.com/am/04/cmpublic/closing.pdf

Lisa Change, Selena L. LaCroix, et al., Whistle While You Work: Ethical, Fiduciary, & Other Dilemmas Facing Over SOX'ed In-house Lawyers, 2004 ACC Annual Meeting presentation, available at http://www.acca.com/am/04/cm/308.pdf

Margaret M. Forman, Kerry A. Galvin, et al., Defining the Role of In-house Lawyers in Governance, 2004 ACC Annual Meeting presentation, available at http://www.acca.com/am/04/cm/711.pdf

Other Resources

- ABA Model Rules of Professional Conduct, at Rule 1.13: Organization as Client, available at: http://www.abanet.org/cpr/mrpc/new_rule1_13.pdf
- ABA Model Rules of Professional Conduct, at Rule 1.6: Confidentiality of Information, available at: http://www.abanet.org/cpr/mrpc/new_rule1_6.pdf
- American Bar Association's Revised Model Rules of Professional Conduct 1.6 & 1.13, News Release (August 20, 2003), available at: http://www.acca.com/protected/comments/professionalconduct.pdf
- ABA Adopts New Model Rules Affecting In-House Practice, News Release, ACCA (August 15, 2003), available at: http://www.acca.com/protected/comments/abamodelrules.pdf
- Brett B. Coffee, Professionals, Core Values and Sarbanes-Oxley: A Critique, The Attorney-CPA (Oct. 2004)
- Kathryn M. Fenton, Counseling the Corporation Post-Sarbanes-Oxley: Ethics and Professionalism Issues For In-house and Outside Counsel, Jones Day, available at: http://www.acca.com/protected/legres/corpresp/counselingcorporation.pdf
- Phillip E. Karmel, Bryan Cave LLP, SEC Disclosure Requirements for Environmental Liabilities and the Impact of Sarbanes-Oxley Act, Practicing Law Institute, 499 PLI/Real 203 (November 2003)
- Giovanni P. Prezioso, Public Statement by SEC Official: Letter Regarding Washington State Bar Association's Proposed Opinion on the Effect of the SEC's Attorney Conduct Rules, Gen. Couns. Mem. (July 23, 2003) available at: www.sec.gov/news/speech/spch072303gpp.htm
- Securities and Exchange Commission Final Rule: Implementation of Standards of Professional Conduct for Attorneys, 17 C.F.R. pt. 205 (2002), available at: http://www.sec.gov/rules/final/33-8185.htm
- Laurence Stuart, In-House Counsel as Corporate Cop–Up the Ladder or Down the Chute, (Baker & McKenzie 2003), available at: http://www.acca.com/protected/legres/ethics/corpcop.pdf

XIII. Sample Policies

A. Sample: Procedures For Complaints Regarding Accounting, Internal Accounting Controls Or Auditing Matters[102]

Introduction

The Audit Committee of Company, Inc. (the "Company") seeks to facilitate disclosure regarding accounting and auditing matters, encourage proper individual conduct and alert the Audit Committee to potential problems relating to accounting or auditing matters before they have serious consequences. Accordingly, the Audit Committee has established the following procedures for the receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls or auditing matters, and for the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters.

Procedures for Complaints

A. Scope of Matters Covered by These Procedures

These procedures relate to complaints or concerns regarding accounting, internal accounting controls or auditing matters of the Company ("Complaints"), including, without limitation, the following:

- fraud or deliberate error in the preparation, evaluation, review or audit of any financial statement of the Company;
- fraud or deliberate error in the recording or maintaining of financial records of the Company;
- deficiencies in or noncompliance with the Company's internal accounting controls;
- misrepresentations or false statements to or by an officer of the Company or an accountant regarding a matter contained in the financial records, financial reports or audit reports of the Company; or
- deviation from reporting of the Company's financial condition as required by applicable laws and regulations.

B. Submission and Receipt of Complaints

1. In General

A person with a Complaint should promptly report the Complaint in writing to the Company's General Counsel. Complaints may, however, be submitted telephonically or in person. Electronic submissions may be emailed to [_____@companyname.com]. The General Counsel will maintain the confidentiality and anonymity of persons making Complaints to the fullest extent reasonably practicable within the legitimate needs of law and any ensuing evaluation or investigation.

2. Anonymous Complaints Hotline

Employees who have Complaints may, rather than submitting such Complaints directly to the General Counsel, submit them confidentially and anonymously by contacting [Anonymous Complaints Hotline Provider]. [Provider] is an independent third party that the Company has hired to receive anonymous Complaints from Company employees and coordinate the delivery of such Complaints to the Audit Committee or appropriate Company personnel. [Provider] may be reached by telephone at _____. The address for writing to [Provider] is: _____ _____. Employees may also contact [Provider] by e-mail at _____.

C. Content of Complaints

To assist the Company in the response to or investigation of a Complaint, the Complaint should be factual rather than speculative, and contain as much specific information as possible to allow for proper assessment of the nature, extent and urgency of the matter that is the subject of the Complaint. It is less likely that the Company will be able to conduct an investigation based on a Complaint that contains unspecified wrongdoing or broad allegations without verifiable evidentiary support. Without limiting the foregoing, the Complaint should, to the extent possible, contain the following information:

- the alleged event, matter or issue that is the subject of the Complaint;
- the name of each person involved;
- if the Complaint involves a specific event or events, the approximate date and location of each event; and
- any additional information, documentation or other evidence available to support the Complaint.

D. Retention of Complaints

Written copies of all Complaints shall be kept in a Complaint file. [Copies of Complaints and the Complaint file shall be maintained in accordance with the Company's document retention policy.]

E. Treatment of Complaints

A copy of all Complaints shall promptly be forwarded to the Audit Committee. The General Counsel shall evaluate each Complaint and may, in consultation with the Audit Committee, conduct an investigation based upon a Complaint. The Audit Committee may, in its discretion, appoint a person other than the General Counsel to initiate and direct an investigation, including an outside attorney or consultant. The Audit Committee may, at any time, request a briefing regarding any investigation of a Complaint and any findings regarding a Complaint. The Audit Committee shall have full authority to determine the corrective action, if any, to be taken in response to a Complaint and to direct additional investigation of any Complaint.

F. Confidentiality/Anonymity

The Company shall maintain the confidentiality or anonymity of the person making the Complaint to the fullest extent reasonably practicable within the legitimate needs of law and of any ensuing evaluation or investigation. Legal or business requirements may not allow for complete anonymity. Also, in some cases it may not be possible to proceed with or properly conduct an investigation unless the complainant identifies himself or herself. In general it is less likely that an investigation will be initiated in response to an anonymous Complaint due to the difficulty of interviewing anonymous complainants and evaluating the credibility of their Complaints. In addition, persons making Complaints should be cautioned that their identity might become known for reasons outside of the control of the Company. The identity of other persons subject to or participating in any inquiry or investigation relating to a Complaint shall be maintained in confidence subject to the same limitations.

G. Protections from Retaliation

Employees are entitled to protection from retaliation for having, in good faith, made a Complaint, disclosed information relating to a Complaint or otherwise participated in an investigation relating to a Complaint. The Company shall not discharge, demote, suspend, threaten, harass or in any manner discriminate against an employee in the terms and conditions of employment based upon any lawful actions of such employee with respect to good faith reporting of Complaints, participation in a related investigation or otherwise as specified in Section 806 of the Sarbanes-Oxley Act of 2002. An employee's right to protection from retaliation does not extend immunity for any complicity in the matters that are the subject of the Complaint or an ensuing investigation.

These procedures are in no way intended to limit the rights of employees to report alleged violations relating to accounting or auditing matters to proper governmental and regulatory authorities.

B. Sample: Whistle Blowing Policy and Procedures[103]

It is the policy of _____Corporation and that of its Board of Directors that no employee shall be discharged or discriminated against with respect to compensation, terms, conditions or privileges of employment because the employee (or any person acting pursuant to the request of the employee) informs either management, the Board of Directors, the Securities and Exchange Commission, or the U. S. Attorney General regarding a possible violation of any law or regulation by the Company or any director, officer or employee, or for expressing any concerns about any questionable accounting, internal accounting controls or auditing matters.

In connection with the above, the Audit Committee of the Board of Directors has established the following procedures:

Under the Code of Ethical Conduct, employees are encouraged to discuss any concerns they have regarding compliance with laws and regulations or other violations of the Code of Ethical Conduct, directly with their manager or, in the alternative, with the General Counsel, who acts as the Company's ethics officer. However, employees may also submit at any time any concerns regarding questionable accounting, internal accounting controls or auditing matters, or any other possible violations of law, by submitting them anonymously in writing to "Executive Offices - Internal Communications", _____. Communications addressed in this manner will be opened by the Company's Assistant Secretary, who will discard the envelope without reading the contents and then forward the contents to the Corporate Secretary. The Corporate Secretary will review the contents and report on them directly to the Audit Committee of the Board of Directors.

In the alternative, employees or third parties who wish to express any concerns directly to the Board of Directors may do so by sending them in writing addressed to "Non-management Directors", care of the Corporate Secretary at the Company's headquarters at_____.

The Corporate Secretary will document and retain all complaints or concerns expressed by employees or third parties regarding possible violations of law or questionable accounting, internal accounting controls or auditing matters and shall report such complaints or concerns directly to the Audit Committee of the Board of Directors.

C. Sample "Up-the-ladder" Company Policy[104]

Date: June 4th, 2005

Subject: Sarbanes-Oxley "Up the Ladder" Reporting

From: The Office of the General Counsel

To: All Members of the Company Legal Team

As you all are aware, Section 307 of the Sarbanes-Oxley Act required the U.S. Securities and Exchange Commission ("SEC") to adopt "standards of professional conduct for attorneys."

The SEC has issued final rules, codified at 17 CFR Part 205, which become effective August 5, 2003. The full text of the rules is available at www.sec.gov/rules/.

This memo is for the purpose of making you aware of these rules and informing you of Company's (including any subsidiary) policies in this regard.

1. The SEC rule requires attorneys who become aware of "evidence of a material violation" by the company or "any officer, director, employee or agent" of the company to report that matter as required by the rule. See 17 CRF § 205.3(b)(1).

2. There are two alternative methods of reporting set forth in the rules.

A. An attorney should report evidence of a material violation to a "supervisory attorney." For Johnson Controls, this would mean that outside counsel and our in-house Group Counsels, Staff Attorneys or other attorneys should report violations to the appropriate business unit General Counsel. A list of the business unit General Counsels with contact information, is attached. If the business unit General Counsel cannot provide an "appropriate response" within a reasonable time, either the business unit General Counsel or the reporting attorney should report the matter to the Office of General Counsel of the Corporation.

B. An attorney may also report evidence of a material violation directly to the Qualified Legal Compliance Committee (QLCC) of the Board of Directors. A list of the current members of this committee is also attached. Although the QLCC is an alternative allowed under the rules, it is our expectation (and strong preference), that most matters be reported up through the Law Department as outlined in the first alternative.

3. The SEC rule applies to all in-house lawyers employed by Johnson Controls, Inc. or any of its subsidiaries and to U.S. admitted outside counsel. There are certain exceptions which may exempt non-US admitted outside counsel. However, the principles reflected in the new SEC rule are consistent with Johnson Controls' policy and we expect our outside lawyers in all jurisdictions to report matters of serious concern they encounter in the course of their representation to appropriate members of JCI management and to the local representative of the JCI Law Department.

4. We will require annual certifications from all of our in-house attorneys that they are familiar with the SEC rules (as amended and modified from time to time) and agree to abide by them. Please sign the attached certification and return it to Sue Christianson by September 30, 2005.

Person, Senior Vice President,

Person, Deputy General Secretary and General Counsel Counsel and Assistant Secretary

D. Up-The-Ladder-Chart Under Sarbanes-Oxley[105]

Endnotes

[1] This information was orginally compiled by Laura Martino, Esq., and updated by Jeanine Mazzorana Esq., at the direction of the Association of Corporate Counsel.

[2] Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (2002) (hereinafter cited by section), available at: http://www.acca.com/legres/enron/sarbanesoxley.pdf.

[3] See In re Enron Corp. Securities, Derivative & ERISA Litigation, (S.D.Tex. 2003) available at 2003 WL 230688 (dismissing charges against Temple). See In re Enron Corp. Securities, 235 F.Supp.2d 549, 684-85 (S.D.Tex. 2002). See AOL and Time Warner Executives Accused of Pocketing Nearly $1 Billion in Insider Trading; Media Giant Inflated Stock Prices With 'Tricks, Contrivances and Bogus Transactions' While Top Executives Hastily Cashed in Their Shares for Personal Profits, Ascribe News, April 13, 2003 available at 2003 WL 5500512. See Jason Hoppin, GC Faces Fraud Charges in the McKesson Case, Prosecutors Allege Active Participation by Top Lawyer, Legal Times, June 16, 2003, Vol. 26, No. 24.

[4] See ACCA Memorandum from Michaela Allbee, Jeffrey M. Smith, and John K. Villa, Recent Proposals for Changes in Corporate Governance, Public Auditing, and the Role of Corporate Counsel: An Update as of July 26, 2002, available at http://www.acca.com/public/reference/enron/acca_update.pdf (noting how the Act passed the House by 423-3 and the Senate by 99-0).

[5] Sarbanes-Oxley Act of 2002, § 307 available at: http://www.acca.com/legres/enron/sarbanesoxley.pdf

[6] Securities and Exchange Commission Final Rule: Implementation of Standards of Professional Conduct for Attorneys, 17 C.F.R. pt. 205 (2002), (hereinafter cited by section) available at: http://www.sec.gov/rules/final/33-8185.htm.

[7] "Washington Metropolitan Area Corporate Counsel Association: Understanding the NEW SEC Attorney Responsibility Rules," Wilmer, Cutler & Pickering (February 6, 2003), available at: http://www.acca.com/chapters/program/wmacca/307rules.pdf.

[8] Giovanni P. Prezioso, Public Statement by SEC Official: Letter Regarding Washington State Bar Association's Proposed Opinion on the Effect of the SEC's Attorney Conduct Rules, Gen. Couns. Mem. (July 23, 2003), available at: www.sec.gov/news/speech/spch072303gpp.htm.

[9] See 17 C.F.R. pt. 207, § 205.1, Purpose and Scope, available at: http://www.sec.gov/rules/final/33-8185.htm.

[10] See Fidelity Fed Sav. & Loan Ass'n. v. de la Cuesta, 458 U.S. 141, 155 (1982) (holding that where an agency regulation permits conduct while state law is prohibits such action, state law is preempted because its prohibition removes the "flexibility" provided by the agency's regulation).

[11] See ABA Model Rules of Professional Conduct (hereinafter ABA Model Rules), Rule 1.6: Confidentiality of Information, (ABA) (August 2003), available at: http://www.abanet.org/cpr/mrpc/new_rule1_6.pdf.

[12] See ABA Model Rule Rules, Rule 1.13: Organization as Client, (ABA) (August 2003) available at: http://www.abanet.org/cpr/mrpc/new_rule1_13.pdf.

[13] Id.

[14] See 17 C.F.R. pt. 207.

[15] Jon Hurdle, Stronger in-house counsel a growing need for business, Philadelphia Business Journal, (Feb. 18, 2005).

[16] SEC §205.1 provides in part: "These standards supplement applicable standards of any jurisdiction where an attorney is admitted or practices and are not intended to limit the ability of any jurisdiction to impose additional obligations on an attorney not inconsistent with the application of this part. Where the standards of a state or other United States jurisdiction where an attorney is admitted or practices conflict with this part, this part shall govern"; See also Implementation of Standards of Professional Conduct for Attorneys, Release Nos. 33-8185, 34-47276 (Jan. 29th, 2003) available at ww.sec.gov/rules/final/33-8185.htm

[17] 17 C.F.R. pt. 207, §§205.2(c), 205.2(g), 205.2(h).

[18] Stephen M. Cutler (Director of the Division of Enforcement of the SEC), "The Themes of Sarbanes-Oxley as Reflected in the Commission's Enforcement Program." Speech delivered before the UCLA School of Law, (September 20, 2004), available at: www.sec.gov/news/speech/spch092004smc.htm.

[19] 17 C.F.R. pt. 207.

[20] 17 C.F.R. pt. 207, §§205.1 and 205.2 (c).

[21] Securities Act of 1933, 15 U.S.C.A. §77a, at §12 (1933).

[22] Securities Act of 1933, 15 U.S.C.A. §77a, at §15(d) (1933).

[23] 17 C.F.R. pt. 207, § 205.2(h).

[24] Id.

[25] Broc Romanek and Kenneth B. Winer, The New Sarbanes-Oxley Attorney Responsibility Standards," ACCA Docket 21 no. 5 (May 2003): 40-55, available at: http://www.acca.com/protected/pubs/docket/mj03/standard1.php.

[26] Id.

[27] Id.

[28] 17 C.F.R. pt. 207, §205.2(g).

[29] Id.

[30] Id.

[31] Xerox Corporation Policy Statement, Office of General Counsel Policy Compliance with SEC Attorney Conduct Standards (August 1, 2003), available at: http://www.acca.com/protected/policy/conduct/xerox.pdf.

[32] Mike Stenglein, Independent Audit Committees and Risks to General Counsel, Corporate Counsel (Feb. 17, 2005), available at: http://www.law.com/jsp/cc/pubarticleCC.jsp?id=1108389926758

[33] 17 C.F.R. pt. 207, §205.3(b).

[34] 17 C.F.R. pt. 207, §205.3(b)(3).

[35] 17 C.F.R. pt. 205.3(b)(1).

[36] 17 C.F.R. pt. 207, §205.3 (b)(1).

[37] 17 C.F.R. pt. 207, §205.2(e).

[38] Id.

[39] 68 Fed. Reg. at 6302.

[40] 17 C.F.R. pt. 207, §205.2(i).

[41] 68 Fed. Reg. at 6302.

[42] Id.

[43] 17 C.F.R. pt. 207, §205.2(d).

[44] Jenny E Cieplak, Michael K. Hibey, The Sarbanes-Oxley Regulations and Model Rule 1.13: Redundant or Complementary, The Georgetown Journal of Legal Ethics, (Summer 2004).

[45] Giovanni P. Prezioso, Public Statement by SEC Official: Letter Regarding Washington State Bar Association's Proposed Opinion on the Effect of the SEC's Attorney Conduct Rules, Gen. Couns. Mem. (July 23, 2003), available at: www.sec.gov/news/speech/spch072303gpp.htm.

[46] John K. Villa, A First Look at the Final Sarbanes-Oxley Regulations Governing Corporate Counsel, Ethics & Privilege, ACCA Docket 21, no. 4(April 2003):90-99, available at: http://www.acca.com/protected/pubs/docket/am03/ethics2.php.

[47] 17 C.F.R. pt. 207, §205.2(e) (defining standard of "evidence of a material violation means credible evidence, based upon which it would be unreasonable, under the circumstances, for a prudent and competent attorney not to conclude that it is reasonably likely that a material violation has occurred, is ongoing, or is about to occur).

[48] See id. (explaining in commentary that it has rejected the standard requiring lawyers to "know" that the conduct is a violation of law or legal duty to the corporation, in favor of a reasonably likely standard, which the SEC describes as "more than a mere possibility but it need not be 'more likely than not.")

[49] See ACCA Memo, What Legal Departments Can Do to Prepare for Compliance with New SEC Rules, available at: http://www.acca.com/protected/article/corpresp/8krule.pdf

[50] ABA Model Rules, Rule 1.13: Organization as Client, cmt 3.

[51] Steven N. Machtinger and Dana A. Welch, In-house Ethical Conflicts: Recognizing and Responding to Them, ACC DOCKET 22, no. 2 (February 2004).

[52] SEC Press Release, "SEC Charges Google and Its General Counsel David C. Drummond with Failure to Register over

$80 in Employee Stock Options Prior to IPO" (January 13, 2005).

[53] Reporting Up the Ladder: Unclear Case Law Creates Tough Decisions, Corporate Legal Times, vol. 15, no. 163 (June 2005).

[54] Jay K. Musoff and Adam S. Zimmerman, The Changing Role of the General Counsel, New York Law Journal (August 6, 2004).

[55] 17 C.F.R. §205.2(b) (e.g., the company has substantially implemented any remedial recommendations made by the selected reviewing attorney after a reasonable investigation and evaluation of the reported evidence). The reporting attorney has advised the corporation that s/he may assert a colorable defense on behalf of the company in any investigation or judicial or administrative proceeding relating to the reported evidence of a material violation. Id.

[56] Broc Romanek and Kenneth B. Winer, The New Sarbanes-Oxley Attorney Responsibility Standards, Acca Docket (May 2003), available at: http://www.acca.com/protected/pubs/docket/mj03/standard2.php

[57] Fact Sheet, Quinn Emanuel Urquhart Oliver & Hedges, LLP, Attorney-Client Privilege in the Corporate Setting 25, available at: http://www.acca.com/chapters/socal/program/corpattyclient.pdf

[58] See Section 205.3(c)(1) and (c)(2).

[59] 17 C.F.R. pt. 207 §205.2(k)(2).

[60] 17 C.F.R. pt. 207 §205.2(k)(3).

[61] 17 C.F.R. pt. 207 § 205.2(k)(4)

[62] 17 C.F.R. pt. 207 § 205.2(k).

[63] See 17 C.F.R. pt. 207, §205.2(k)(4); See also, Joseph T. McLaughlin, Guy N. Molinari, Karen M. Crupi-Fitzgerald, and Holly Kulka, Qualified Legal Compliance Committee: Policies and Procedures, Heller Ehrman White & McAuliffe LLP, 3-16, (April 2003), available at: http://www.acca.com/protected/program/qlcc_presentation.pdf (interpreting QLCC powers and responsibilities).

[64] 17 C.F.R. §205.2(k).

[65] See Simon M. Lorne, An Issue-Annotated Version of the Sox, A Work in Progress, Munger, Tolles & Olson LLP, (December 2003), available at: http://www.acca.com/protected/article/corpresp/sarbox_attyethics.pdf.

[66] See Joseph T. McLaughlin, Guy N. Molinari, Karen M. Crupi-Fitzgerald, and Holly Kulka, Qualified Legal Compliance Committee: Policies and Procedures, Heller Ehrman White & McAuliffe LLP 14 (April 2003), available at: http://www.acca.com/protected/program/qlcc_presentation.pdf (interpreting QLCC powers and responsibilities).

[67] Susan Hackett Memo to ACCA Members, Issues for Law Departments Considering Whether to Recommend that Their Board Create a CLCC (August 27, 2003), available at: http://www.acca.com/protected/article/corpresp/qlcc_issues.pdf.

[68] Jill Fisch, The Qualified Legal Compliance Committee: Using The Attorney Conduct Rules To Restructure The Board Of Directors, Duke Law Journal, Vol. 53, No. 2, (2005)

[69] See id. (criticizing the structure of QLCC).

[70] Id.

[71] More information and discussion about the Sarbanes-Oxley Act, please visit ACC Corporate Responsibility page at www.acca.com/legres/corpresponsibility/index.php and the SEC Final Rules at http://www.sec.gov/rules/final/34-49412.htm [

[72] See Emerging and Leading Practices in Sarbanes 307 Up-The-Ladder Reporting and Attorney Professional Conduct Programs: What Companies and Law Firms are Doing, Leading Practice Profiles Series, ACCA (September 4, 2003), available at: http://www.acca.com/protected/article/corpresp/lead_sarbox.pdf

[73] 18 U.S.C. 1514A.

[74] 18 U.S.C. § 1513(e).

[75] Welch v. Cardinal Bankshares, Corp., Case No. 2003-SOX-15 (U.S. DOL ALJ Jan. 28, 2004)

[76] Kathleen Day, Whistle-Stop Campaigns: Some Firms Are Trying to Limit Protection of Workers Who Express Wrongdoing, The Washington Post, F1 (April 23, 2006).

[77] Adam Geller, Judge Orders Reinstatement for First Sarbanes-Oxley Whistleblower, AP News (Feb. 23rd, 2005), available at: http://www.law.com/jsp/article.jsp?id=1108992919634

[78] In-house counsel would not have been required to "withdraw from representing the issuer and notify the SEC within one business day of such withdrawal and indicate that the

TELGIAN
STANDARD POLICY

1.0 Policy

Telgian will conduct every international business transaction with integrity, regardless of differing local manners and traditions, and will comply with:

(a) The laws and regulations of the United States, particularly the provisions of the Foreign Corrupt Practices Act (FCPA)

(b) The laws and regulations of each foreign country in which the Corporation operates (except to the extent inconsistent with US law)

(e) The Corporation's Code of Ethics and Business Conduct.

If there is a real or apparent inconsistency between the requirements of US and foreign law, the matter will be resolved by the General Counsel.

2.0 General

2.1 This policy applies to all officers and employees of the Corporation and its wholly-owned subsidiaries, both within and outside the US, and, by written agreement, flowing down all appropriate provisions to all distributors, and to all consultants, agents, representatives, brokers or other persons or firms of US or any other nationality who have or are likely to have contact with a foreign customer and are hired or otherwise retained by the Corporation to provide services directly related to obtaining, retaining, or facilitating business or business opportunities, including offset/countertrade commitments to foreign governments, in or with any foreign country or foreign firm ("consultants").

3.0 Implementation

3.1 A brief description of the FCPA is set forth in Exhibit A, Description of the Foreign Corrupt Practices Act. 3.2 It is the individual responsibility of each officer, employee, and consultant of the Corporation, by action and supervision as well as continuous review, to ensure strict compliance with this policy. The Corporation may take severe disciplinary action, up to and including dismissal, against any officer, employee, or consultant who violates this directive.

3.3 Any officer or employee who suspects or becomes aware of any violation of this policy must report the violation to the General Counsel, who will cause an investigation of the reported matter to be conducted. In the alternative, any officer, employee, or consultant who suspects or becomes aware of any violation of this policy may report it directly to the General Counsel.

3.4 The General Counsel is responsible for furnishing advice with respect to the interpretation and application of the FCPA and of this policy. He or she also will assist each business area in ensuring that affected personnel are fully informed of the prohibitions of the FCPA and the requirements of this policy.

3.5 Each business area is responsible for ensuring that all affected business area personnel are fully informed of the prohibitions of the FCPA and the requirements of this policy. In addition, he or she is responsible for adopting and enforcing appropriate controls and taking

the steps necessary to effect compliance with this policy by all officers, employees, distributors, and consultants of the Corporation in the business area.

3.6 Exceptions to this policy must have prior written approval of the General Counsel. Exceptions will not be granted unless legal opinions have been obtained from outside counsel that the conduct for which approval is sought does not violate applicable US or foreign law.

Description of the Foreign Corrupt Practices Act
Exhibit A of

1.0 Accounting and Recordkeeping Controls Requirements
The FCPA requires certain US companies to establish accounting and recordkeeping controls that will prevent the use of "slush funds" and "off-the-books" accounts which have been used in the past by some companies as a means of facilitating and concealing questionable foreign payments. In particular, the FCPA requires companies to establish and keep books, records, accounts, and controls which accurately and fairly reflect their transactions and disposition of their assets.
2.0 Anti-Bribery Provisions (Prohibitions)
The FCPA, as amended in 1998, prohibits US persons (and non-US persons while in the United States) from corruptly offering or giving money or anything of value, directly or indirectly through agents or intermediaries, to foreign officials to assist the US (or non-US) person in "obtaining or retaining business." Specifically, the FCPA prohibits any act corruptly done in furtherance of an offer, payment, promise to pay, gift, promise to give, or authorization of the giving of "anything of value" to:

(a) Any foreign official (see paragraph6.1)

(b) Any foreign political party or official thereof or any candidate for foreign political office, or

(c) Any person (including any consultant), while knowing (or being aware of a high probability) (see paragraph 6.3for the FCPA's knowledge standard) that all or a portion of such money or thing of value will be offered, given or promised, directly or indirectly, to any foreign official, any foreign political party or official thereof, or any candidate for foreign political office for purposes of:

(i) Influencing any act or decision in his, her, or its official capacity (or in the case of a foreign official, inducing him or her to do or omit to do any act in violation of that official's lawful duty)

(ii) Inducing him, her, or it to use his, her, or its influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality, or

(iii) Securing any improper advantage (e.g., obtaining a special tax exemption or operating permit for a factory which otherwise would not qualify)

in order to assist in obtaining or retaining business for or with, or directing business to, any person.
3.0 Limited Exceptions and Affirmative Defenses
The FCPA contains certain limited exceptions and affirmative defenses to the prohibitions set forth in section 2.0 above.

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3.1 *Facilitating Payments*
3.1.1 The FCPA provides that the prohibitions referred to in section 2.0 above do not apply to any facilitating or expediting payment to any foreign official, political party, or party official, "the purpose of which is to expedite or secure performance of a routine governmental action."
3.1.2 Examples of such "routine governmental action(s)" include actions ordinarily and commonly performed by a foreign official in:

(a) Obtaining permits, licenses, or other official documents to qualify a person to do business in a foreign country

(b) Processing governmental papers such as visas and work orders

(c) Providing police protection, mail pickup and delivery, or scheduling inspections associated with contract performance or inspections related to transit of goods across country

(d) Providing phone service, power and water supply, loading and unloading cargo, or protecting perishable products or commodities from deterioration, or

(e) Actions of a similar nature.

3.1.3 The term "routine governmental action" does not include any decision by a foreign official on whether, or on what terms, to award new business to or continue business with a particular party, or any action taken by a foreign official involved in the decision-making process to encourage a decision to award new business or to continue business with a particular party.
3.2 *Affirmative Defenses*. The FCPA also contains two affirmative defenses for: (a) "reasonable and bona fide" expenditures, such as travel and lodging expenses, incurred by or on behalf of a foreign official, party, party official, or candidate that are directly related to the promotion, demonstration, or explanation of products or services or the execution or performance of a contract with a foreign government or agency thereof; or (b) payments to foreign officials that are lawful under the written laws and regulations of the foreign official's country.
4.0 Penalties - Fines and Imprisonment
The FCPA's penalties for violation of the anti-bribery provisions include fines of up to $2,000,000 per violation for companies and fines of up to $100,000 and/or imprisonment for up to five years per violation for individuals. The FCPA prohibits a company from reimbursing a director, officer, employee, or consultant for the amount of the fine involved. Individuals are subject to criminal liability under the FCPA regardless of whether the company has been found guilty or prosecuted for a violation.
5.0 Applicability
5.1 As amended in 1998, the jurisdictional reach of the FCPA extends to "any person," including any foreign person or firm, that commits a prohibited act in the United States. The FCPA thus applies to foreign nationals, foreign corporations (including foreign subsidiaries of US companies), and other foreign entities whose directors, officers, employees, or agents commit a corrupt act while in the United States.
5.2 The FCPA, as amended, also applies to US nationals and US companies that commit prohibited acts outside the United States, regardless of the use of any instrumentality of interstate commerce. Thus, a US company may be held liable for the acts of its directors,

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officers, employees or agents (including its foreign subsidiaries) outside the United States, regardless of the nationality of the person taking the action and regardless of the use of an instrumentality of interstate commerce.
5.3 A US company may be held vicariously liable under the FCPA for the corrupt conduct of its foreign subsidiaries outside the United States if the US company authorized or participated in the conduct. Any US national who is a director, officer, employee or agent of a foreign subsidiary may also be held liable under the FCPA for acts in furtherance of the bribery of a foreign official, whether or not such acts are performed within or outside the territory of the United States.

6.0 Key Terms

6.1 As used in this policy, "foreign official" means any officer or employee of a foreign government, its armed forces, or any department, agency, or instrumentality thereof, or any person acting in an official capacity for or on behalf of such government or department, agency, or instrumentality, or any official, employee or person acting on behalf of a public international organization such as the World Bank or the European Community.
6.2 The prohibition against payments to foreign officials extends to the offering or giving of "anything of value" where the requisite criminal intent and business purpose are present. The thing of value given can be of any kind, not just money, and there is no minimum amount or threshold of value which must be exceeded before the gift becomes illegal.
6.3 The FCPA specifically defines the degree of knowledge necessary for a violation. Under the FCPA, "knowing" conduct requires an awareness or a firm belief that the agent, representative, or other third party is making a corrupt payment, or a substantial certainty that this will occur. The FCPA knowledge standard is also met where there is awareness of a high probability that the corrupt payment will be made, unless there is actual belief to the contrary. Willful ignorance (sticking one's head in the sand) is not excused. There may be circumstances in which a director, officer, employee, or consultant of the Corporation becomes aware of facts which, while in and of themselves do not cause the individual either to know or believe that a foreign official will be the ultimate recipient of a bribe, should cause suspicion. In these circumstances, if the individual fails to take steps to allay that suspicion, he or she may risk prosecution under the FCPA, as the director, officer, employee, or consultant may be accused of having had the requisite knowledge for a violation.
6.4 Although the FCPA does not define "instrumentality" of a foreign government, the term should be construed to include entities which are wholly- or partially-owned by a foreign government, such as the Saudi Arabian Airlines Corporation (Saudia) or a specially chartered private corporation entrusted with quasi-governmental functions, as well as organizations such as ARABSAT, because the majority of the membership of those organizations is composed of foreign governments and quasi-governmental entities. An entity partially-owned by a foreign government will be deemed to be an "instrumentality" for FCPA purposes under this policy when the foreign government holds the majority of the entity's subscribed capital, controls the majority of the votes attached to the shares issued by the entity, or can appoint the majority of the entity's administrative or managerial body or supervisory board. An entity also will be deemed to be an "instrumentality" under this policy where the foreign government has a significant ownership interest representing less than a majority but is the single largest shareholder, has the power to appoint board members (less than a majority), combined with negative veto powers, and has the power to exercise effective or de facto control.

FCPA PROBLEM

As Associate General Counsel for International Operations, Joe Champion is counsel for all overseas activity of his company, Building Products International (BPI). BPI has a very lean in-house counsel team, with no one permanently posted overseas. Local, outside counsel are rarely used in an effort to keep costs to a minimum; virtually all legal work is done at headquarters.

Due to the rapid growth of infrastructure projects around the world, BPI has experienced tremendous expansion of its business around the world, but especially in Africa. International business now accounts for nearly sixty percent (60%) of the company's revenue; of that amount, African business totals nearly half, or twenty nine per cent (29%), of the company's revenue.

The CEO, Bill Bucks, founded the company and has been leading it since it went from a privately held business to one that is now listed on the NY Stock Exchange. His mission in life is BPI, demanding growth in the business quarter-over-quarter. Everyone is measured by and rewarded on revenue and profit growth. And, BPI has had an unbroken record of growth and timely filing of all its reports and disclosures.

Yesterday, three weeks before the company's 10-K is due to be filed and the analysts' conference call is scheduled, Joe Champion got a troubling phone call from the one of BPI's African business managers, Jim Hope, questioning the reported figures. Hope told Champion that a substantial number of sales have been booked well in advance of having executed contracts or delivery of products; he said that the pressure to exceed prior reported figures was intense and that there was no legitimate way to do so.

Furthermore, Hope reported that several important government customers had cooperated by submitting orders which were clearly excessive and would have to be significantly modified after the close of the reporting period. In return, those individual government officials "were taken care of". Hope said that, for example, he knew one government official was provided a

scholarship for his son to attend school in the US. He was believes that this expenditure was reported as a consulting contract.

Hope said that there had been minor examples of such practice in the past, but now due to some contractual and customer funding problems, BPI Africa was generating and booking revenue virtually any way it could. Hope said that he raised his concerns with the head of BPI Africa, Stan Strong, who told him (Hope) that he did not understand how to book revenue, that the auditors had approved these transactions and that he should not be concerned anymore.

Joe Champion has scheduled an appointment with his boss, the General Counsel Phil Friendly, for today. Champion knows that everyone in the C suite is elated about results as reflected in the draft 10-K. Friendly is especially pleased as he expects to announce his retirement shortly after the filing and collect a substantial bonus as he leaves. Friendly's successor has not been designated at this time.

Discussion Questions:

- What are Champion's specific obligations under SOX?
- Are there any FCPA issues which affect his obligations?
- What does the Attorney Conduct Rule require Champion to do?
- When/How is Champion required to report "Up the Ladder"?
- Is Hope subject to Whistleblower protection? Is Champion?