

Ethical Responsibilities of Legal and Compliance Professionals: Recent SEC and FINRA Cases Involving Lawyers and Compliance Professionals¹

Summary

In recent years, there has been only one action against a lawyer by the SEC, and none by self regulatory organizations (“SROs”) like FINRA, where the alleged misconduct is primarily or solely based on an ethical breach. Although there have been a few such actions against compliance professionals, they typically involve other misconduct. However, as regulators focus on individual culpability and alleged conflicts of interest which may contribute to investor harm, it is possible that legal and compliance professionals at regulated broker dealers will come under greater individual scrutiny than in the past.

This article examines some recent cases and the potential legal theories available to the SEC and FINRA to bring action against lawyers and compliance professionals for allegedly unethical or improper conduct.

Two SEC opinions in the past year are worth particular discussion since they provide insight on the SEC’s views about policing unethical conduct. One SEC decision discusses but does not apply the SEC’s Rule of Practice 102(e), which authorizes the SEC to discipline attorneys and accountants found to have “*engaged in unethical or improper professional conduct.*” The second SEC decision, on appeal from an SRO action, confirmed that “*unethical conduct*” by securities professionals violated NYSE Rule 476(a)(6), even in the absence of bad faith. The rule is the predecessor to current FINRA Rule 2010 and is grounded in a longstanding SRO rule that prohibits “*conduct inconsistent with just and equitable principles of trade*” (“J&E Rule”).²

Arguably, these decisions could be read to support SRO action against lawyers and compliance professionals subject to SRO jurisdiction where their allegedly unethical conduct violates industry norms and professional standards. In the past, however, the SEC generally has been reluctant to employ its conduct rule prohibiting unethical conduct by attorneys practicing before the SEC primarily because such actions might deter lawyers from counseling clients in need of advice.

Similarly, extending the reach of the J&E Rule to lawyers and compliance personnel would have a chilling effect on clients’ willingness to seek legal and compliance advice and assistance from in house counsel and compliance officers. The potential for such actions presents an even greater challenge for in house lawyers already juggling their obligations to FINRA as associated persons

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² A third case resulting in the issuance of an initial decision by an SEC Administrative Law Judge (“ALJ”) that a lawyer engaged in unethical and improper unprofessional conduct is also noteworthy although it represents a fairly unique set of facts. *See discussion below re In the Matter of Steven Altman, Esq.*, 2009 SEC LEXIS 1507 (Jan. 14, 2009).

with their ethical obligation to represent their clients aggressively but within the bounds of applicable professional standards.

We submit that the same strong policy reasons behind the SEC's historic reluctance to use Rule 102(e) should apply equally to any SRO effort to apply the J&E Rule to allegedly unprofessional or unethical conduct by legal and compliance officers. An after the fact challenge by the SEC or SROs under either Rule 102(e) or the J&E Rule that legal and compliance officers' failed to meet professional standards of care is fraught with risk for both sides and should be avoided.

SEC Rule 102(e): Policing Attorneys Practices before the SEC

Origins of SEC Rule to Discipline Unethical Attorney Conduct

Since 1935, the SEC has had the authority to discipline unethical attorney conduct. In the past 25 years however, the SEC has almost steadfastly avoided invoking such authority under its Rule of Practice 102(e), 17 CFR 201.102(e), unless the offending conduct clearly violates the federal securities laws.³

The SEC's authority to discipline attorneys appearing before it has sparked controversy for many years, reaching a high point in the 1981 SEC decision in *William R. Carter*, 47 S.E.C. 471 (1981). In that decision, the SEC declined to sanction a lawyer pursuant to former Rule of Practice 2(e) for allegedly aiding and abetting a securities law violation, absent a showing that respondents "*were aware or knew that their role was part of an activity that was improper or illegal.*"⁴

Several years later, the SEC expanded and re-codified Rule 2(e) as current Rule of Practice 102(e), so as to retain the right to censure an attorney or otherwise deny or curtail the "*privilege of appearing or practicing before it,*" not only in instances where the SEC found the attorney had willfully violated or willfully aided or abetted a violation of the federal securities laws, but also in cases where such individuals were found "*(i) not to possess the requisite qualifications to*

³ The SEC has never hesitated to charge lawyers with willful violations or willful aiding and abetting violations all types of misconduct, ranging from insider trading to violations in connection with the unregistered offering of securities. *See, e.g., SEC v. Rasch*, No. 09-cv-1190 (N.D. Ga. filed May 5, 2009) (attorneys charged with violating Section 10(b) and Rule 10b-5 for conducting a fraudulent legal "*opinion mill*"); *In the Matter of Trautman Wasserman & Co., Inc.*, (Admin. Proc. File No. 3-12559, Feb. 14, 2008) (compliance officer charged with aiding and abetting violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder); *SEC v. Guttenberg*, No. 07- CV- 1774 (S.D.N.Y. filed Mar. 1, 2007) (compliance attorney charged with insider trading). At times, the attorney's misconduct arose from their role as counsel and/or their access to information given their special status. *See, e.g., In the Matter of Benjamin G. Sprecher*, 52 S.E.C. 1296 (1997) (attorney found to have "*masterminded*" elaborate fraud and evasion of the registration requirements); *U.S. v. O'Hagan*, 521 US 642 (1997) (insider trading by lawyer who became privy to client's non-public intent to acquire a public company); *SEC v. Fehn*, 97 F.3d 1276 (9th Cir. 1996) (attorney found to have substantially assisted client in preparation of misleading disclosure statements); *SEC v. Electronics Warehouse, Inc.*, 689 F. Supp. 53 (D. Conn. 1988) (attorney found to have recklessly violated Section 17 of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5).

⁴ *Carter*, 47 S.E.C. at 504.

*represent others; or (ii) to be lacking in character or integrity or to have engaged in unethical or improper professional conduct.”*⁵

Despite insisting that it possessed the authority under Rule 102(e) to pursue unethical conduct by lawyers, the SEC has continued to exercise restraint in applying its terms absent evidence that an attorney has engaged in a substantive violation of the federal securities laws. In fact, we could find only one case in which the SEC asserted solely the provisions of Rule 102(e)(1)(i) or (ii) as a basis for discipline, in a case with fairly unique facts concerning the alleged obstruction of an SEC administrative hearing by a lawyer charged with attempting to extort a payment from the respondent in exchange for his client’s not making herself available to testify against the respondent. *In the Matter of Steven Altman, Esq.*, 2009 SEC LEXIS 1507 (Jan. 14, 2009).

Altman: ALJ Sanctions Lawyer for Attempting to Thwart SEC Proceedings

Altman was an initial decision issued by Chief ALJ Brenda Murray on January 14, 2009 after a contested hearing. The ALJ found that Altman, while representing a witness in an SEC administrative hearing against her former employer, violated Rule 102(e) and certain canons of the New York State Code of Professional Responsibility and Disciplinary Rules when he knowingly contacted counsel for her employer and “*offered to have his client act in ways that would thwart the Commission’s prosecutorial activities in exchange for benefits for his client. By seeking benefits for a client in exchange for behavior and/or testimony by the client that would adversely impact a Commission administrative proceeding, Altman engaged in conduct that involved dishonesty, fraud, deceit, and misrepresentation.*”⁶

According to the decision, Altman had several telephone conversations with the respondent’s counsel to resolve certain financial issues on behalf of his client, after learning that she would be called by the SEC Enforcement staff (“Division”) to testify against the respondent, intimating that her availability and memory might be affected favorably toward the respondent if her outstanding financial issues were resolved. Respondent’s counsel rejected the overtures and secretly recorded the conversations. When the Division called Altman’s client as a witness (unaware that Altman had contacted respondent’s counsel), respondent’s counsel presented the tapes at the SEC proceeding and successfully impeached the witness. The SEC subsequently brought a proceeding against Altman alleging his conduct violated Rule 102(e). After a hearing, the ALJ rejected all of Altman’s arguments with regard to the enforceability of Rule 102(e) and ordered that he be suspended from practice before the SEC for 9 months.

Prior to *Altman*, the SEC had not initiated an enforcement proceeding against an attorney for an ethical breach for many years. In fact, in a decision six months before the ALJ decision in *Altman*, the SEC strongly signaled its reluctance to use Rule 102(e) absent conduct that violated the federal securities laws in a case on appeal where the attorney respondent was not even charged with a violation of Rule 102(e). *In the Matter of Scott G. Monson*, 2008 SEC LEXIS 1503 (June 30, 2008).

⁵ 17 CFR 201.102 (e)(1)(i) and (ii) (emphasis added).

⁶ *Altman*, 2009 SEC LEXIS at *66.

Monson: In Defense of a Rule Not Charged

The SEC's apparent reluctance to invoke the rule was raised obliquely but at great length in *Monson* when it refused to overturn an ALJ's dismissal of a case brought against a lawyer whose allegedly negligent drafting of a market timing agreement was said to have "caused" violations of Investment Company Act ("ICA") Rule 22c-1 by the broker dealer for which the lawyer served as general counsel. According to *Monson*, the terms of the final agreement allowed clients to enter late trades, after the close, and still receive that day's NAV, contrary to ICA Rule 22c-1. The SEC separately sued and obtained judgments and settlements against Monson's firm, its CEO and its head of Operations. Monson contested the charges and after a hearing, the ALJ dismissed all the charges against him. The Division appealed the dismissal to the SEC which reviewed the case *de novo*, affirming the dismissal below.⁷

Although Monson was not charged under Rule 102(e), the Division, on appeal to the full SEC, argued that Monson's lack of knowledge that his acts or omissions would contribute to a violation of Rule 22c-1 was not dispositive of whether he should be found to have contributed to his firm's violation of the pricing rule. In essence, the Division argued that Monson should be sanctioned because his actions as an attorney fell short of the professional standards to which he was subject, a rationale that sounded a lot like the principles underlying Rule 102(e). The three SEC Commissioners who signed the Opinion,⁸ were obviously reluctant to draw that conclusion:

The Division contends that "the ultimate question in determining Monson's negligence," and therefore whether he can be found to have caused his company's violation, "is what a reasonable attorney in Monson's position, acting with due care, would have done." Monson allegedly "failed to conform to basic professional standards regarding competence."

*Thus characterized on appeal, the charges against Monson hinge on his role as a legal advisor to [his firm]. The Division essentially contends that, by not having requisite knowledge of the securities laws and by failing to conduct further legal inquiry regarding trade timing issues in connection with the drafting of the Agreement, Monson was negligent in providing legal advice to his client.*⁹

The Opinion therefore rejected the Division's rationale and concluded that there was insufficient evidence that Monson had acted negligently in drafting the agreement. The SEC did not find that the circumstances surrounding certain changes in the agreement (allowing the client to place late trades), "necessarily should have alerted Monson, given his background and responsibilities, to the need for inquiry."¹⁰ As a result, the SEC sustained the ALJ decision dismissing the charges.

⁷ *Monson*, 2008 SEC LEXIS at *1-4.

⁸ Only three Commissioners participated in the decision: Chairman Cox and Commissioners Atkins and Casey. Of the three, only Commissioner Casey remains.

⁹ *Monson*, 2008 SEC LEXIS at *12-13.

¹⁰ *Id.* at *22.

Monson: SEC Cautions against Disciplining Lawyers Solely for Unethical Breach

Notwithstanding its review of the evidence and conclusion that the Division had failed to prove even negligent conduct by Monson, the Opinion went to great lengths to preserve but refrain from applying the principles behind Rule 102(e). Although Monson was not charged under Rule 102(e), the Commissioners presumably felt compelled to both defend and caution against the rule's application. In doing so, the Opinion reviewed the controversy stemming from the SEC's 1981 decision in *Carter*, its subsequent adoption of Rule 102(e) and its concern that the rule not be invoked in such a way as to chill a lawyer's advocacy or a client's decision to consult counsel when confronted with difficult problems.¹¹

Given how unnecessary the issue was to the holding in *Monson*, the vigor with which the Commissioners defended their restraint is worth consideration. Although quite lengthy, *Monson's* spirited warnings about invoking Rule 102(e) are noteworthy, especially as a backdrop to their consideration of the J&E rule a few months later:

Over twenty-five years ago, in William R. Carter, we recognized particular concerns attendant to disciplining lawyers based on faulty legal advice and noted a distinction between actions with scienter and those without scienter. We held that, to sanction a lawyer pursuant to former Rule of Practice 2(e) for having aided and abetted a securities law violation, the Commission had to show "that respondents were aware or knew that their role was part of an activity that was improper or illegal." In confirming this "intent requirement" for aiding and abetting, we emphasized the "[s]ignificant public benefits [that] flow from the effective performance of the securities lawyer's role." We also recognized that, "[i]n the course of rendering securities law advice, the lawyer is called upon to make difficult judgments, often under great pressure and in areas where the legal signposts are far apart and only faintly discernible." We expressed concern that, to the extent lawyers exercising their professional judgment are excessively motivated by "fear of legal liability or loss of the ability to practice before the Commission," clients may well decide not to consult lawyers on difficult issues.

Given these considerations, we eschewed a standard that would expose an attorney to professional discipline "merely because his advice, followed by the client, is ultimately determined to be wrong." The intent requirement, we said, is crucial to an allegation of wrongdoing by a lawyer because it "provides the basis for distinguishing between those professionals who may be appropriately considered as subjects of professional discipline and those who, acting in good faith, have merely made errors of judgment or have been careless."

For some time after Carter, the Commission exercised restraint under Rule 2(e) by initiating "proceedings against attorneys only where the attorney's conduct has already provided the basis for a judicial or administrative order finding a securities law violation in a non-Rule 2(e) proceeding." When we acknowledged this practice, in connection with a 1988 rulemaking regarding Rule 2(e), we stated that "the Commission, as a matter of policy, generally refrains from using its administrative forum to conduct de novo determinations of

¹¹ Although the ALJ Decision in *Altman* does not reference *Monson*, it considered but rejected many of the same policy arguments, concluding that *Altman's* conduct was so egregious that a finding that he violated Rule 102(e) was amply supported by the record. *Altman*, 2009 SEC LEXIS at *54-59, *76-78.

*the professional obligations of attorneys." We also noted that we sought to "minimize[] the risk . . . that public disciplinary proceedings may have a chilling effect on zealous representation of a client, particularly when the attorney appears before the Commission as an advocate in an enforcement matter." **Consistent with these practices and policies, and with our reasoning in Carter, we have refrained from bringing disciplinary proceedings against lawyers under Rule 2(e) and its successor, Rule 102(e), based on negligent legal advice.***

*Concerns about the scope of liability that have motivated our restraint with respect to Rule 102(e) actions against lawyers similarly are present in litigated administrative enforcement actions such as this case alleging that a lawyer caused another person's violation of the securities laws. **The charges against Monson as framed by the Division – that Monson departed from professional standards of competence in rendering private legal advice to their clients – raise the same risks we identified in Carter and other proceedings: an encroachment by the Commission on regulation of attorney conduct historically performed by the states; interference with lawyers' ability to provide unbiased, independent legal advice regarding the securities laws; and chilled advocacy on behalf of clients in proceedings before the Commission. As far as we are aware, we have not sanctioned attorneys in litigated enforcement proceedings based on alleged negligent acts or omissions they may have committed in providing non-public legal advice to clients.***¹²

As noted, *Monson* was decided by only three Commissioners; two of whom (Chairman Cox and Commissioner Atkins) have since left the SEC. Notwithstanding the ALJ Decision in *Altman* it is unclear whether the SEC under Chairman Mary Schapiro's leadership might deviate from the course articulated in the *Monson* decision, and consider using Rule 102(e) against lawyers. Absent facts as egregious as those alleged in *Altman*, it seems unlikely, given the strong policy reasons expressed in *Monson* even in circumstances where they seem to be dicta.

Rasch: "Operating a Legal Opinion Mill"

A very recent case filed against two lawyers charged with operating a "legal opinion mill," suggests that the under Chairman Schapiro's leadership, the SEC will follow the traditional path where it believes a lawyer's misconduct violates the federal securities laws. The complaint alleges the lawyers' misconduct violated the registration and antifraud provisions of the Securities Act of 1933 and the antifraud provisions of the Securities Exchange Act of 1934 ("Exchange Act"). *SEC v. Rasch*, No. 09-cv-1190 (N.D. Ga. filed May 5, 2009).

According to the *Rasch* complaint, the lawyer defendants and two others (a firm called "144 Opinions Inc." and its non-lawyer principal), collectively issued fraudulent legal opinions used by promoters in a "pump-and-dump" scheme, to sell securities in violation of the registration provisions of the federal securities laws. Rasch and his associate allegedly executed at least 24 legal opinion letters concerning the removal of restrictive legends on certificates representing over 22 million shares of an issuer called Mobile Ready Entertainment Corp. ("Mobile Ready"). The SEC alleged that the defendants cited to non-existent documents and misrepresented critical facts in executing the 24 legal opinions. The complaint alleges that the false and misleading

¹² *Id.* at *13-18 (citations omitted) (emphasis added).

statements were drafted by the non-lawyer defendant who owned defendant 144 Opinions Inc. The legal opinions were thereafter executed by Rasch and his associate, fraudulently inducing the transfer agent for Mobile Ready to remove the restrictive legends and permit the illegal sale of over 22 million shares of Mobile Ready in violation of the registration provision of the federal securities laws.¹³

Although the case does not allege that the lawyer defendants engaged in unethical or unprofessional conduct as defined by Rule 102(e), their alleged role in preparing faulty legal opinions in furtherance of a fraudulent scheme also would seem to fall within the scope of Rule 102(e).¹⁴

FINRA Rule 2010: Conduct Inconsistent with Just and Equitable Principles of Trade

Heath: Unethical Conduct by Securities Professionals is Actionable Under the J&E Rule

Although the SEC may still walk softly around Rule 102(e), a recent decision interpreting the J&E Rule suggests it views an SRO's authority to police unethical professional behavior to be on stronger ground than Rule 102(e). *In the Matter of the Application of Thomas W. Heath, III*, 2009 SEC LEXIS 14 (Jan. 9, 2009), *appeal docketed*, No. 09-0825 (2d Cir. Mar. 3, 2009).¹⁵ It is not clear whether *Heath's* reasoning would sustain the use of the J&E Rule were an SRO to charge a lawyer or compliance professional with unethical behavior, or whether the SEC would consider the policy reasons discussed in *Monson* important enough to curb its use by an SRO against lawyers or compliance officers.

According to the SEC opinion, Heath was an investment banker who, in the course of completing a banking assignment at the firm he was leaving, disclosed the deal he was working on to his future colleague at his new bank, in circumstances where Heath understood the latter would keep the information confidential. Instead, the individual contacted Heath's client and sought a role for himself and his own bank. Both Heath and his "tippee" were fired and Heath's offer of employment at the new firm was rescinded. The NYSE (prior to its merger with the NASD into FINRA) brought an action against Heath for violating the J&E Rule. After a hearing, Heath was found to have violated the J&E Rule and fined \$100,000, although not otherwise

¹³ Complaint for Injunctive and Other Relief at 1-3, *Rasch* (No. 09-cv-1190); *see also SEC v. Rasch*, SEC Litigation Release No. 21024 (May 5, 2009).

¹⁴ The *Rasch* complaint did not allege whether the lawyer defendants "practiced" before the SEC, a typical predicate for invoking Rule 102(e). *But see Altman*, 2009 SEC LEXIS at *15 ("*practicing before the Commission ... is not a requisite for the applicability of Rule 102(e)(1)(ii)*"). It will be interesting to see whether the SEC prosecutes its case by contrasting the lawyer defendants' actions with the professional standards of care to which lawyers typically preparing such opinions are held, as the Division asserted in the *Monson* appeal.

¹⁵ FINRA Rule 2010 (which superseded former NASD Rule 2110) mandates that "[a] member, in the conduct of business, shall observe high standards of commercial honor and just and equitable principles of trade." Correspondingly, NYSE Rule 476(a)(6) calls for the imposition of sanctions upon any individual or entity that is found guilty of "*conduct or proceeding inconsistent with just and equitable principles of trade.*"

Heath was premised on a violation of NYSE Rule 476(a)(6), but the SEC decision addressed the J&E Rule in general.

sanctioned. Heath appealed. As discussed below, the SEC affirmed the violation and the \$100,000 fine. Heath has appealed that decision to the Second Circuit.¹⁶

Heath concerned an investment banker, rather than a lawyer or compliance officer, but the SEC's opinion expressly compared the legal basis on which Rule 102(e) rests to that of the J&E Rule, observing that the J&E Rule "is grounded in an explicit and longstanding statutory mandate," under Section 6(b)(5) of the Exchange Act, which grants SROs the "statutory responsibility to prevent unethical practices among its membership."¹⁷ The opinion did so in a context in which it rejected the appellant's argument that case law under the predecessor to Rule 102(e) cautioned a narrow reading of a rule pertaining to unethical conduct rather than substantive violations. Instead, citing the different statutory basis under which the J&E Rule was adopted, *Heath* held that securities professionals "voluntarily subject [themselves] to [an SRO's] rules" and therefore "recognize [the SRO's] authority 'to discipline their members for unethical behavior as well as violations of law.'"¹⁸

***Heath*: Does it Apply to Lawyers and Compliance Professionals?**

Given the foregoing rationale, it is conceivable that the SEC would be equally supportive of an SRO's effort to police the alleged unethical behavior of an in house lawyer or compliance professional whose conduct did not violate a substantive provision of the SRO rules or federal securities laws, relying on the J&E Rule to do so. While it has not occurred frequently, the SROs have brought cases against compliance officers under the J&E Rule.¹⁹ While their advice is not subject to the attorney client privilege, compliance officers frequently play an advisory role similar to in-house counsel, interpreting complex SEC and SRO requirements and counseling their business colleagues on compliance. Thus the policy reasons to protect their actions from second guessing by regulators are the same as those relating to a lawyer's advice.

At a minimum, there is nothing in *Heath* which excludes lawyers from its reach, despite the fact that a few months earlier in *Monson*, the SEC went to great lengths to cite the policy reasons

¹⁶ *Heath v. SEC*, No. 09-825 (2d Cir. appeal docketed Mar. 3, 2009).

¹⁷ *Heath*, 2009 SEC LEXIS at *33 (quotations omitted).

¹⁸ *Id.*, quoting *Paul K. Grassi, Jr.*, Exchange Act Rel. No. 52858 (Nov. 30, 2005), 86 SEC Docket 2494, 2497.

¹⁹ *E.g.*, *In the Matter of the Application of Robert E. Strong* (Admin. Proc. File No. 3-12599, Mar. 4, 2008) (Strong, the CCO and lone compliance officer, was found responsible for his firm's compliance with certain employee personal trading rules; his failure to detect or prevent trading by a research analyst violated the J&E Rule and was deemed a failure to supervise); *Mutual Services Corporation, Dennis S. Kaminski, Susan Coates, Michael Poston, Denise Roth, Gari C. Sanfilippo, Kevin L. Cohen and J. Graham Taylor*. (FINRA Disc. Proc. No. EAF0400630001, Dec. 16, 2008), *appeal to NAC pending*, <http://www.finra.org/web/groups/industry/@ip/@enf/@adj/documents/ohodecisions/p118006.pdf>. (CCO Poston, Kaminski (his successor as CCO), and other compliance officers held to have violated the J&E Rule and failed to supervise. Poston became aware that trade blotters were not being reviewed in a timely manner but did not take action to address the failure. Supervisors backdated the blotters to give the appearance that they had been reviewed timely. Additionally, Poston modified the firm's Written Supervisory Procedures and directed his assistant to backdate the procedures to make it appear that the firm changed its procedures to include review of a monthly trend report).

why any disciplinary action against a lawyer solely for “*unethical conduct*” should be treated with extreme caution. If, as *Heath* suggests, the J&E Rule extends to all securities professionals, it would seem to apply to lawyers and compliance personnel as well, where they are employed by a member firm.

The SEC’s willingness to apply the J&E Rule liberally and Rule 102(e) sparingly has yet to be reconciled in a case involving lawyers or compliance professionals. Surprisingly, there has been little commentary challenging the SROs application of the J&E Rule to reach the conduct of broker-dealer compliance officers and attorneys. In *Heath*, the SEC reinforced the authority of FINRA and the other SROs to pursue unethical misconduct under the J&E Rule, regardless of whether such activity implicates specific substantive SEC laws and rules or SRO rules.

Importantly, *Heath* held that bad faith need not be found in order to be liable for a violation of the J&E Rule, and the rule “*applies to either conduct committed in bad faith or **conduct violating ethical standards.***”²⁰ The SEC also stated that the J&E Rule “*incorporates broad ethical principles, and focuses on the ethical implications of the applicant’s conduct.*”²¹ Additionally, the SEC concluded that the J&E Rule may be “*fairly applied to conduct that is not ethical and accepted conduct in the securities industry.*”²²

In support of its findings, the SEC stated that Heath had “*violated one of the most fundamental ethical standards in the securities industry.*”²³ Specifically, the SEC pointed out:

“*[a]s an experienced investment banker, Heath can be fairly charged with notice that his breach of his duty to maintain the confidentiality of his client’s information violated the just and equitable principles of trade. Any reasonably prudent securities professional would recognize that the disclosure of confidential client information violates the ethical norms of the industry.*”²⁴

Although few might quarrel with charging an in-house lawyer or compliance officer who made a disclosure like Heath under the J&E Rule, *Heath*’s broad language raises a concern that any conduct deemed unethical or in breach of professional standards might be actionable, even if such behavior did not otherwise violate substantive SEC or SRO law and was not done in bad faith. Since lawyers and compliance officers may provide counsel which turns out to be mistaken—but in good faith—will the SROs be tempted to second guess their advice and invoke the J&E Rule against them?

The SEC’s ringing endorsement of the J&E Rule to police unethical conduct therefore raises a question about its potential use to police the ethical responsibilities of, and potential conflicts of interest relating to, broker-dealer legal and compliance personnel. It also raises the question

²⁰ *Heath*, 2009 SEC LEXIS at *15 (emphasis added).

²¹ *Id.* at *13 (internal quotations omitted).

²² *Id.* at *28 (internal quotations omitted).

²³ *Id.* at *10.

²⁴ *Id.* at *29.

whether the SEC, if presented with the same facts as those in *Monson* or *Rasch* on appeal in an SRO case, would sustain a charge under the J&E Rule.

Conclusion

The SEC appears far more comfortable applying the J&E Rule in circumstances where a securities professional engages in unethical conduct that breaches professional standards than the SEC has been in applying its own disciplinary rule to police unethical conduct by lawyers. Hopefully, were FINRA or another SRO to pursue lawyers or compliance professionals under the J&E Rule, the SEC would recall its own words in *Carter* and *Monson*, that more harm than good might come from second-guessing such professionals' judgments or conduct after the fact:

*We also recognized that, "[i]n the course of rendering securities law advice, the lawyer is called upon to make difficult judgments, often under great pressure and in areas where the legal signposts are far apart and only faintly discernible." We expressed concern that, to the extent lawyers exercising their professional judgment are excessively motivated by "fear of legal liability or loss of the ability to practice before the Commission," clients may well decide not to consult lawyers on difficult issues.*²⁵

However different the origins of SEC Rule 102(e) and the J&E Rule, the chilling effect on legal and compliance officers were they to be the subject of an action would be the same.

²⁵ *Monson*, 2008 SEC LEXIS at *13-14.