



California Corporate & Securities Law

SEC's Whistleblower Release Misapprehends California Ethics Laws And Rules

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In a 3–2 vote yesterday, the Securities and Exchange Commission approved [final rules](#) implementing the whistleblower provisions of Section 21F of the Securities Exchange Act of 1934.

The more law, the greater the injustice

The adopting release is 305 pages long and has 83,917 words, or just about five hundred more words than Nathaniel Hawthorne's 1850 masterpiece novel, *The Scarlet Letter* (83,421 words). This reminds me of a line from a book that the great Roman lawyer Marcus Tullius Cicero wrote to his son in the last year of his life – *De Officiis* (On Duties). In Chapter 33, Cicero quotes what was then (43 B.C.) a common proverb, “Summum ius summa iniuria” or “the more the law, the greater the injustice”.

Internal compliance programs undermined

In my [comments](#) on the proposed rules, I wrote:

An enforcement-only approach to securities regulation is neither effective nor practical. The Commission should adopt rules that encourage voluntary compliance. Compliance is only possible when issuers have effective compliance, legal and audit programs. These programs will be materially undermined if persons who become aware of possible violations have a substantial monetary incentive to bypass those programs.

The SEC did not heed these or numerous other similar comments. SEC Chairwoman Mary Schapiro acknowledged that “no issue received more focus during this process than the role of internal compliance programs.” She argued that the final rules provide expanded incentives for whistleblowers to report internally. In my view, these incentives are likely to be largely ineffective in encouraging internal reporting.

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Release misapprehends ethical obligations of California lawyers

As a California attorney, I note that the adopting release evidences a real misunderstanding of the ethical obligations of lawyers. For example, the release refers to “applicable state statutes or bar rules governing the ethical behavior of attorneys” and cites only California Evidence Code § 956. The statute cited, however, establishes an exception to an evidentiary privilege. In California, an attorney’s ethical obligations are established by the [Rules of Professional Conduct](#) and the State Bar Act (found in the California Business & Professions Code).

While this may seem academic, the rules of evidence and the statutes and rules governing attorney conduct are not the same. Business & Professions Code § 6068(e) requires (with one very limited exception) an attorney to “maintain inviolate the confidence, and *at every peril* to himself or herself to preserve the secrets, of his or her client”. This statutory duty to maintain a client confidences is broader than the attorney–client privilege which is subject to numerous exceptions.

In 2004, I participated as a member of the drafting committee of the Corporations Committee of the Business Law Section of the California State Bar in writing an article for the [Pepperdine Law Review](#) that analyzes this issue at some length: [Conflicting Currents: The Obligation to Maintain Inviolable Client Confidences and the New SEC Attorney Conduct Rules](#), 32 Pepp. L. Rev. 89 (2004).

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