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The Risks of Overzealous Advocacy in SEC Proceedings

By Joshua Horn – 06/09/2011

The movies often wrongfully portray lawyers as smooth talking mouth pieces who will do or say anything for their clients, regardless if that conduct crosses the line of decency and ethics. Unfortunately, the recent comments of the Securities and Exchange Commission's Director of Enforcement Robert Khuzami reflect that fiction may, in fact, be reality when it comes to the conduct of certain lawyers before the agency. Although Director Khuzami acknowledged that lawyers should be zealous and aggressive advocates for their clients and that such advocacy can lead to success before the SEC, he noted that there are certain types of conduct that the SEC considers questionable at best and, in turn, may lead to undesired results. Among other things, Khuzami stated that this conduct causes delay, increases expense and thwarts the investigative process, resulting in injustice.

One problem the SEC has noted is multiple representations of witnesses with adverse interests. A related but different issue, Khuzami observed, is multiple witnesses represented by the same lawyer who all adopt the same implausible explanation of events. Khuzami stated that the SEC frequently sees one lawyer representing multiple witnesses, even thought those witnesses may have

adverse interests. For example, the SEC has observed one lawyer representing the supervisor and the person supervised in a "failure to supervise" case. With respect to lawyers engaged in this practice, Khuzami noted that the SEC's new Cooperation Program raises the stakes because it provides for reduced or no sanctions in exchange for truthful and substantial assistance. As such, the SEC is taking a much closer look at multiple representation. In certain instances, the SEC has asked a witness to confirm that counsel has informed the witness of the potential conflict of interest, and that the witness has willingly chosen to go through with the engagement. Khuzami stated that, when conflicts come to pass after this multiple representation, the SEC is less likely to extend any courtesies to the witness or subsequent counsel.

The next issue that the SEC has observed is when a witness answers "I don't recall" dozens of times, even to the most basic questions. Although Khuzami recognized that memories fade over time, making the "I don't recall" answer proper, Khuzami described the problem as one where a witness employs this answer in response to the most basic questions, such as when a witness was asked to describe his job. According to Khuzami, this failure of recollection is not only incredible but also implausible. As a result, the SEC will likely draw an adverse inference from such testimony. The SEC finds this lack of recollection even more problematic when the witness continues to lack recollection even after being shown contemporaneous documents that the witness herself authored. In one case, the SEC observed a highly placed and accomplished executive over the course of a two-day examination, involving high-intensity issues in which he was personally involved, claim a lack of recollection. This same person asserted that his memory was not refreshed even though he spent fifteen hours preparing with his lawyer. Surprisingly, the SEC has observed the same "lack of recollection" witness have perfect recollection when the questioning turned to facts favorable to the witness.

One of the more troubling observations that Khuzami had involved a lawyer signaling her client. Signaling ranges from the more basic, such as a long

speaking objection, to more outrageous, as when a lawyer tapped his client's foot in response to certain questions. When confronted, the foot-tapping lawyer denied such conduct. When questioning resumed, however, the SEC watched the witness extend his leg out completely searching for his lawyer's foot tap signal, until finally realizing that the lawyer now had both feet tucked firmly under his chair.

Khuzami's final observation addressed issues with document production. For example, the SEC has observed a practice of delayed production until immediately before an examination, thwarting the SEC's preparation. Equally troublesome from Khuzami's standpoint is the over-inclusive claim of privilege, only to then have the documents released after the examinations are completed, requiring the SEC to decide whether to recall a witness.

Lawyers may ask, what is the risk of being this type of zealous advocate? Khuzami spelled that out in his comments. Among other things, a lawyer could be barred from practiced before the SEC. In addition, he stated that the SEC is not shy about referring the matter to the Department of Justice for obstruction of justice and perjury, including false claims of a lack of recollection. Equally important, Khuzami noted that referral to enforcement is based, in part, on the credibility of opposing counsel. In the end, the overly zealous and obstructive lawyer may do her client a disservice. Khuzami further observed that obstructive practices are particularly risky in light of the SEC's new Whistleblower Program and Cooperation Program, which only lends credence to the possibility that an insider with intimate knowledge of the truth will come forward.

The biggest takeaway for all lawyers who practice before the SEC, can be found in Khuzami's closing remarks: "Lawyers contemplating sharp practices should ask themselves what kind of reputation, and what level of credibility, they want to have with the staff, and whether that matters to them -- and to their clients." All of us lawyer who practice before the SEC should heed these words, lest we turn fiction into reality.

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