No. 09-525

In the Supreme Court of the United States

JANUS CAPITAL GROUP INC., ET AL., PETITIONERS

v.

FIRST DERIVATIVE TRADERS

*ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT*

BRIEF FOR ATTORNEYS' LIABILITY ASSURANCE SOCIETY, INC., A RISK RETENTION GROUP, AS AMICUS CURIAE SUPPORTING PETITIONERS

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INTEREST OF AMICUS CURIAE

Founded in 1987, Attorneys' Liability Assurance Society, Inc., A Risk Retention Group (ALAS), is the Nation's leading provider of professional liability insurance for large law firms. ALAS is a mutual insurance company that insures 236 major law firms, including approximately 60,000 lawyers in 45 States and the District of Columbia—approximately one out of every thirteen lawyers in private practice.

Lawyers from ALAS's loss-prevention staff were actively involved in the American Law Institute's development of the Restatement (Third) of the Law Governing Lawyers and in the American Bar Association's recent revision of the Model Rules of Professional Conduct, and they are involved with many other professional and bar associations that have defined the ethical and professional duties of lawyers. Among other services, ALAS provides its insured attorneys with extensive loss-prevention advice, and it is widely recognized as the leader in that area. As part of its responsibilities, ALAS monitors the defense of professional liability claims asserted against its member firms and lawyers. By virtue of the many services it renders, ALAS has a unique understanding of the problems confronting law firms today. To this end, ALAS has filed amicus briefs addressing issues of vital concern to the Nation's legal community.

This case presents such an issue. ALAS's insured attorneys have advised virtually every significant public company in the United States and have provided legal services to public companies in connection with countless securities offerings. In recent years, plaintiffs have increasingly sought to pursue securities-fraud claims against law firms and lawyers as a result of the provision of those services, even though lawyers are the quintessential example of secondary actors. ALAS files this amicus brief to bring to the Court's attention the consequences of extending securities-fraud liability to lawyers for the advice they provide to their clients—which would harm both the legal profession and the clients it serves.[1]

[1] Pursuant to Rule 37.6, ALAS affirms that no counsel for a party authored this brief in whole or in part; no such counsel or a party made a monetary contribution to fund its preparation or submission; and no person other than ALAS, its members, or its counsel made such a monetary contribution. The parties have consented to the filing of this brief, and copies of their letters of consent are on file with the Clerk's Office. Counsel for ALAS also represents some of ALAS's members individually in other litigation, including securities litigation.

SUMMARY OF ARGUMENT

A. The issue whether lawyers can be subject to liability for securities fraud typically arises in the context of documents issued by public companies in connection with securities offerings. Although lawyers are often involved in the preparation of those documents, their role is usually a circumscribed one, and lawyers do not sign filings made with the Securities and Exchange Commission (SEC). Instead, lawyers directly speak to the public only through opinion letters that state specific legal opinions about the company or the securities being offered. To date, the courts of appeals have consistently held that lawyers cannot be liable under the securities laws for misrepresentations by their clients, but can be liable for misrepresentations made by, and attributed to, the lawyers themselves.

B. In deciding this case, the Court should make clear that lawyers, as outside service providers, can be liable only for attributed statements. The attribution rule flows directly from the language both of Section 10(b) and of Rule 10b-5. And it is also rooted in the reliance requirement, an essential element of the private right of action under Section 10(b). When a statement is issued by a company, the market rightly presumes that the statement is being "made" by the company, not by an outside service provider such as a lawyer. The practical consequences of a contrary rule would be to permit a private right of action for aiding and abetting against secondary actors such as lawyers and to introduce uncertainty and inconsistency in the application of the securities laws to those actors.

C. A rule that permitted the imposition of securities liability on lawyers and law firms without attribution would have devastating consequences for the legal profession. It would render it virtually impossible for a defendant lawyer or law firm to obtain early dismissal of a private securities-fraud action—and would thereby expose lawyers to the onerous burdens of discovery. Unlike other defendants, moreover, law firms have only a limited ability to settle securities litigation, because law-firm partners are highly mobile and have limited incentives to remain with a firm that is about to pay a sizable settlement. And although lawyers and law firms would initially bear the brunt of liability under any more expansive standard for private securities-fraud actions, the eventual burden would fall on clients and the public at large.

D. Finally, a broader liability rule would disrupt the attorney-client relationship and chill the provision of legal services. Lawyers are not "gatekeepers" of their clients and are not required to investigate their activities. Making lawyers liable for their clients' public statements would effectively impose such a gatekeeping obligation and upset lawyers' professional and ethical obligations to their clients. Lawyers may react to a broader liability rule, moreover, simply by refusing to represent "high-risk" clients, such as newer and smaller companies or companies on the verge of bankruptcy. And a broader liability rule is simply unnecessary to effectuate the remedial goals of the securities laws, because the SEC has the authority to pursue lawyers for aiding and abetting securities fraud and lawyers have powerful incentives not to engage in such misconduct. In sum, extending liability to lawyers for mere participation in the preparation of statements made by their clients would serve little purpose and would work great mischief.

ARGUMENT

LAWYERS CANNOT BE LIABLE IN A PRIVATE ACTION UNDER SECTION 10(b) AND RULE 10b-5 FOR STATEMENTS THAT ARE NOT ATTRIBUTED TO THEM

ALAS agrees with petitioners that, under a proper understanding of the securities laws, petitioners, as mere advisers, should not be liable for statements made in prospectuses by the mutual funds they advised, on the ground that those statements were not attributed to them. ALAS files this amicus brief in order to explain why the Court should make clear that lawyers, as outside service providers, cannot be liable for unattributed statements.

A. Lawyers, Like Other Outside Service Providers, Often Advise Clients In The Preparation Of Their Public Disclosures

1. The issue of whether lawyers can be subject to liability for securities fraud typically arises in the context of documents issued by public companies in connection with securities offerings. Those documents are typically prepared through a collaborative process involving corporate executives and employees; internal legal and accounting personnel; and the company's outside service providers, consisting of lawyers, accountants, and sometimes other consultants. See generally 2 Ronald E. Mallen & Jeffrey M. Smith, *Legal Malpractice* § 14:6, at 502-503 (West, 2010 ed.).

As a result, it is rarely the case that a single person, much less a single person outside the company, is responsible for any particular document or section thereof. For example, a public filing typically contains a summary presentation of the company's financial data. Information for that presentation ordinarily comes from the business units involved; a group within the corporation aggregates that information into an initial draft; corporate executives and external and internal counsel will consider revisions to the language; and other executives and external and internal accountants will revise and update the financial information to be included in the filing. As the draft is updated, that process is reiterated. See, *e.g.*, Final Report of Court-Appointed Examiner, App. C, at 82-87, *In re Enron Corp.*, No. 01-16304 (Bankr. S.D.N.Y. Nov. 14, 2003) (Enron Report).

2. Outside legal counsel are most frequently consulted not about specific data, but rather about nuanced questions concerning statements in the filing or the company's reporting obligations more generally. In those circumstances, outside counsel, taking the facts as given, are called upon to advise clients on legal issues as to which the law is not yet settled and reasonable minds could differ as to the correct outcome. In the ordinary case, securities lawyers will devote their attention to complicated legal questions against the backdrop of a relatively small body of facts that inform the analysis on a particular question; they may sometimes be asked to do so where the underlying factual information is either incomplete or in a state of flux. See Association of the Bar of the City of New York, *Report by Special Committee on Lawyers' Role in Securities Transactions*, 32 Bus. Law. 1879, 1884-1886 (July 1977); Robert J. Haft & Michele H. Hudson, *Due Diligence—Periodic Reports & Securities Offerings* § 1:1, at 3 (2009-2010 ed.) (Haft & Hudson); 2 Michael J. Halloran et al., *Venture Capital & Public Offering Negotiation* 36-6 (3d ed. 1997 & Supp. 2009); Thomas D. Morgan, *Sarbanes-Oxley: A Complication, Not a Contribution, in the Effort to Improve Corporate Lawyers' Professional Conduct*, 17 Geo. J. Legal Ethics 1, 26-27 (2003) (Morgan).

It is therefore rare for outside counsel to develop first-hand knowledge of the business or accounting information that constitutes the core of most disclosures by public companies, including the periodic filings made by those companies with the Securities and Exchange Commission (SEC). Lawyers usually do not have expertise regarding the business or accounting matters discussed in the disclosures. As a result, they ordinarily do not study or confirm the factual information contained therein; that is the job of corporate executives and accountants. And it would not be cost-effective for clients to educate lawyers on those matters, because an understanding of those matters is not essential to the performance of their duties. See Morgan 24-25.

For major disclosures, such as a company's annual Form 10-K filing with the SEC, the company's executives directly sign the filing, pursuant to applicable legal requirements. See 15 U.S.C. 77f(a); 17 C.F.R. 240.13a-14, 240.15d-14. Outside accountants also sign a report stating the results of their audit of the company's financial statements. See 17 C.F.R. 210.2-02; *United States* v. *Arthur Young & Co.*, 465 U.S. 805, 810-811 (1984). Outside counsel, by contrast, do not themselves sign SEC filings. At most, in connection with some public filings (typically initial filings for the issuance of new securities), outside counsel issue a signed opinion letter that states specific legal opinions about the company or about the securities being offered. See, *e.g.*, *Legal Opinion Letters: A Comprehensive Guide to Opinion Letter Practice* §§ 6.2-6.5, at 6-3 to 6-29 (M. John Sterba, Jr., ed., Aspen Publishers 3d ed. 2003 & Supp. 2004) (*Legal Opinion Letters*); Haft & Hudson § 6:2, at 204-208. Law firms carefully vet those opinion letters, which are attributed to the lawyers themselves, before they are issued; firms expend considerable resources verifying the contents of those letters, and many firms have permanent committees that review opinion letters before they are issued in the firms' names. See *Legal Opinion Letters* § 1.6, at 1-21 to 1-23; 1 Gary Lawrence, *Due Diligence in Business Transactions* § 5.13[1] (Law Journal Press 2010).

3. In light of the secondary role outside counsel play in the preparation of public companies' disclosures, the courts of appeals have consistently held that outside counsel cannot be liable under the securities laws for misrepresentations by their clients in those statements. See, *e.g.*, *Pacific Investment Mgmt. Co.* v. *Mayer Brown LLP*, 603 F.3d 144, 161 (2d Cir. 2010) (*PIMCO*) (holding that a law firm was not liable for misrepresentations in a client's SEC filings and offering documents); *Ziemba* v. *Cascade Int'l, Inc.*, 256 F.3d 1194, 1205-1206 (11th Cir. 2001) (holding that a law firm was not liable for misrepresentations in a client's press release and letters); *Schatz* v. *Rosenberg*, 943 F.2d 485, 497 (4th Cir. 1991) (holding that a lawyer had no duty to disclose a client's misrepresentations when the lawyer "did no more than 'paper the deal' ").

By contrast, courts of appeals have held that outside counsel can be liable where the lawyers undertake to speak directly to a third party or to the public at large: for example, by issuing an opinion letter. See, *e.g.*, *Thompson* v. *Paul*, 547 F.3d 1055, 1063 (9th Cir. 2008) (endorsing view that "[a]n attorney who undertakes to make representations to prospective purchasers of securities" can be liable for those representations); *Rubin* v. *Schottenstein, Zox & Dunn*, 143 F.3d 263, 266-268 (6th Cir. 1998) (en banc) (holding that a lawyer can be liable for the substance of conversations the lawyer had with investors); *Kline* v. *First Western Gov't Securities, Inc.*, 24 F.3d 480, 485-486 (3d Cir. 1994) (holding that a law firm can be liable for an opinion letter containing misrepresentations).

B. Lawyers, Like Other Outside Service Providers, Cannot Be Liable In A Private Action For Statements That Are Not Attributed To Them

In dismissing claims brought against lawyers and other service providers in a private action under Section 10(b) and Rule 10b-5, lower courts have relied on the "attribution" rule: *i.e.*, the rule that, in order for an outside service provider to be liable for its role in assisting in the preparation of an alleged misstatement, the statement must be attributed to it. See, *e.g.*, *PIMCO*, 603 F.3d at 161 (holding that "[s]econdary actors * * * can be held liable in a private damages action brought pursuant to § 10(b) and Rule 10b-5(b) only for false statements attributed to the secondary actor at the time of dissemination"); *Lattanzio* v. *Deloitte & Touche LLP*, 476 F.3d 147, 153 (2d Cir. 2007) (explaining that "a plaintiff must allege a misstatement that is attributed to the [service provider] at the time of its dissemination, and cannot rely on the [service provider's] alleged assistance in the drafting or compilation of a filing") (internal quotation marks omitted); *Ziemba*, 256 F.3d at 1205-1206 (rejecting claim against a law firm that allegedly played a "significant role in drafting, creating, reviewing or editing allegedly fraudulent letters or press releases" where that role was never disclosed to investors) (internal quotation marks omitted). The attribution rule is grounded in the language of Section 10(b) and Rule 10b-5; the reliance requirement applicable to private Section 10(b) actions; and important public-policy considerations underlying the securities laws. Because the court of appeals' "implicit attribution" rule cannot be reconciled with the attribution rule as properly understood, this

Court should reject that rule—particularly as it is applied to outside service providers such as lawyers.

1. The attribution rule flows directly from the language of Section 10(b) itself, which renders it unlawful for any person to "use or employ * * * any manipulative or deceptive device or contrivance" in connection with the purchase or sale of securities. 15 U.S.C. 78j(b). One does not "use or employ" a statement when one has merely "participated * * * in [its] drafting," as the government proposes. U.S. Cert. Br. 11. As this Court has previously acknowledged in another context, the "ordinary or natural" meaning of "use" is to "convert to one's service," "employ," "avail oneself of," or "carry out a purpose or action by means of." *Bailey* v. *United States*, 516 U.S. 137, 145 (1995) (internal quotation marks and alterations omitted). All of those definitions denote "action and implementation." *Ibid.* Outside service providers such as lawyers do not "convert" a client's statements to their own "service"; to the contrary, it is the *client* that "avail[s] [it]self" of the *lawyer's* work. To say that a lawyer "use[s] or employ[s]" the client's statements to the marketplace is to turn the meanings of those terms on their heads.

Although the language of Section 10(b) is itself unambiguous, the language of Rule 10b-5 confirms the point. The provision of Rule 10b-5 on which respondents rely makes it unlawful for any person to "make any untrue statement of a material fact." 17 C.F.R. 240.10b-5(b). As a matter of plain language, it is fundamentally different to "make a statement" than it is to "participate[] to a sufficient degree in the drafting or dissemination" of a statement. U.S. Cert. Br. 11. Put simply, to "make a statement" is to *speak* (or to be the attributed speaker of) the statement—not merely to have participated in the creation of a statement that is spoken by (or attributed to) someone else. Cf. *Stoneridge Inv. Partners, LLC* v. *Scientific-Atlanta, Inc.*, 552 U.S. 148, 157 (2008) (noting that an element of a claim under Rule 10b-5 is a "material misrepresentation or omission *by the defendant*") (emphasis added). For example, no one would say that President Reagan's famous statement, "Mr. Gorbachev, tear down this wall," was "made" by his speechwriter, Peter Robinson—even though Robinson drafted the statement. See Peter Robinson, *It's My Party: A Republican's Messy Love Affair with the GOP* 13, 16 (2000). And even if the language of Rule 10b-5 could be read differently, Rule 10b-5 cannot prohibit conduct that Section 10(b) itself does not. See, *e.g.*, *Central Bank of Denver, N.A.* v. *First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 173 (1994).

2. The attribution rule is also rooted in the "essential element of the § 10(b) private cause of action" that a private plaintiff must establish reliance. *Stoneridge*, 552 U.S. at 159. In order to satisfy the reliance requirement, the plaintiff must show that he "in fact rel[ied] upon [the defendant's] *own* deceptive conduct." *Id.* at 160 (emphasis added). The necessary corollary of that principle is that, when a plaintiff brings suit against an outside service provider such as a lawyer, the plaintiff must plead and prove that he relied on the service provider's "*own* deceptive statements." *PIMCO*, 603 F.3d at 155-156.

That corollary is hardly a surprising one, because, when one considers whether to rely on a statement (particularly a financial statement), one naturally considers who is making it: *i.e.*, to whom the statement is attributed. See *id.* at 156. It would greatly matter to an investor whether a description of a company's business is being made by the chief executive officer (who should know the company better than anyone) or instead by an outside service provider (whose knowledge of the company may be partial or specialized). And when a statement is issued by a company, the market rightly presumes that the statement is being "made" by the company, not by an outside service provider—even where the outside service provider is identified in the company's disclosures (and the market is therefore aware of the provider's involvement). See *In re Refco, Inc., Securities Litig.*, 609 F. Supp. 2d 304, 313-314 (S.D.N.Y. 2009), aff'd, *PIMCO*, *supra*; Ben D. Orlanski, Comment, *Whose Representations Are These Anyway? Attorney Prospectus Liability After 'Central Bank,'* 42 UCLA L. Rev. 885, 945 (1995) (Orlanski) ("Who else can be said to represent something in a prospectus if not the company selling its securities?").

As was true with the counterparty to the transaction at issue in *Stoneridge*, moreover, nothing that an outside service provider does makes it "necessary or inevitable" that the provider's client will make a particular statement. *Stoneridge*, 552 U.S. at 161. Even assuming there were ever a situation in which outside counsel singlehandedly drafted a statement that their client then signed and issued, the ultimate decision whether to issue the statement would be made by the client; the client would retain the right to change the statement or simply to issue it as is. See Orlanski 946 (noting attorneys "lack the ultimate authority to control the contents of the prospectus"). And it would presumably be the client that asked for the statement to be prepared in the first place. Even if counsel's involvement in the preparation of the statement was substantial, therefore, there can be no reliance on outside counsel's own conduct as long as the statement is attributed to the client company—and outside counsel thus cannot be liable in a private action under Section 10(b).

3. Important public-policy considerations also support the application of the attribution rule to outside service providers such as lawyers.

a. This Court held in *Central Bank* that a private party may not pursue a Section 10(b) action against a secondary actor on a theory of aiding and abetting liability. See 511 U.S. at 191. In the wake of *Central Bank*, Congress considered, and rejected, a proposal to create an express right of action for aiding and abetting under Section 10(b); instead, Congress chose to authorize only the SEC to seek civil redress against aiders and abettors. See, *e.g.*, 15 U.S.C. 78t(e); S. Rep. No. 98, 104th Cong., 1st Sess. 19 (1995). Allowing liability for a primary violation in the absence of attribution would "revive in substance" private claims against aiders and abettors and would thereby circumvent the congressional judgment not to permit liability in those circumstances. *Stoneridge*, 552 U.S. at 162.

Notably, the government's proffered standard proves as much. The government suggests that a party other than an issuer can be liable for a misstatement where the party merely "participate[s] to a sufficient degree in [its] drafting." U.S. Cert. Br. 11. Yet that is merely aiding and abetting by another name. See, *e.g.*, *Shapiro* v. *Cantor*, 123 F.3d 717, 720 (2d Cir. 1997) (noting that "[a]llegations of 'assisting,' 'participating in,' 'complicity in,' and similar synonyms * * * all fall within the prohibitive bar of *Central Bank*").

b. In defining the contours of liability under Section 10(b) and Rule 10b-5, moreover, this Court has repeatedly emphasized the need for "certainty and predictability" in the rules governing liability. *Central Bank*, 511 U.S. at 188 (quoting *Pinter* v. *Dahl*, 486 U.S. 622, 652 (1988)). The attribution rule directly supports that need. The great virtue of the attribution rule is that it provides clarity to outside service providers such as lawyers. Under the attribution rule, lawyers know that, if statements are attributed to them (as in opinion letters), they will potentially be exposed to securities liability; if statements are not attributed to them, they will not. Lawyers can structure their services accordingly. The attribution rule is easy not only to understand, but also to apply: the issue of attribution can usually be resolved on the face of the pleadings or of the documents referenced therein.

By contrast, any alternative standard, such as the "sufficient participation" standard advanced by the government or the "implicit attribution" standard applied by the court of appeals, affirmatively disserves the need for certainty and predictability. For its part, when the SEC first addressed the issue in the wake of *Central Bank*, it expressly rejected a "*substantial* participation" standard as too "susceptible to misinterpretation"; instead, it advanced a standard under which a person could be liable if he "creates" the statement in question. See SEC Br. at 18-19, *Klein* v. *Boyd*, Nos. 97-1143 & 97-1261 (3d Cir. April 1998) <www.sec.gov/pdf/klein.pdf>. More recently, however, the SEC took a seemingly more expansive view of its "creator" standard, suggesting that a person can be liable for "creating" a statement where the person simply "provides the false or misleading information that another person then puts into the statement." SEC Br. at 7, *PIMCO*, *supra* (Aug. 6, 2009). In ultimately refusing to hold a law firm liable in that case for misrepresentations in a client's filings, the Second Circuit rejected the SEC's standard; in so doing, it observed that "[e]ven the SEC struggles to define the precise contours of [its] creator standard." *PIMCO*, 603 F.3d at 157.

The government now explicitly acknowledges that it favors some form of standard in which "participation" in the creation of a statement is sufficient to give rise to primary liability. The government continues to struggle, however, to explain what that standard actually means. The government asserts that a statement made under a company's own name "may" give rise to liability—but makes no effort to explain when it does and when it does not. See U.S. Cert. Br. 16 n.7. Instead, the government seemingly suggests that whether participation is sufficient to give rise to primary liability is an issue of fact, potentially to be resolved by a jury at trial. See *ibid.* (noting that "[c]ontemporaneous attribution may also be relevant to *proving* that a particular entity 'made' an alleged misstatement") (emphasis added). But this Court has previously rejected such a "shifting and highly fact-oriented" standard for the imposition of liability in a private action under Section 10(b). *Central Bank*, 511 U.S. at 188 (quoting *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 755 (1975)).

The court of appeals' "implicit attribution" standard fares no better in this regard. By the court of appeals' own admission, that standard mandates a "case-by-case" inquiry into whether "interested investors would attribute to the defendant a substantial role in preparing or approving the allegedly misleading statement." Pet. App. 24a. Like the government's "sufficient participation" standard, therefore, that standard would leave for the factfinder the determination as to whether a given fact pattern is sufficient to give rise to primary liability. As a result, application of that standard, like the government's standard, would lead to "the undesirable result of decisions made on an ad hoc basis, offering little predictive value to those who provide services to participants in the securities business." *Central Bank*, 511 U.S. at 188 (internal quotation marks and citation omitted).

Such amorphous standards are not a "satisfactory basis for a rule of liability imposed on the conduct of business transactions." *Central Bank*, 511 U.S. at 188 (quoting *Blue Chip Stamps*, 421 U.S. at 755).[2] Rather than adopting such a standard here, the Court should make clear that, at least with regard to outside service providers such as lawyers, a provider may be primarily liable for a misstatement only where the misstatement has been attributed to it.

C. A Rule That Permitted The Imposition Of Securities Liability On Lawyers And Law Firms Without Attribution Would Have Devastating Consequences

While both Congress and this Court have recognized that "litigation under Rule 10b-5 presents a danger of vexatiousness different in degree and in kind from that which accompanies litigation in general," *Blue Chip Stamps*, 421 U.S. at 739,[3] lawyers and law firms are particularly vulnerable to the pernicious consequences of securities litigation. A relaxation of the previously settled attribution rule would expose lawyers and law firms to those consequences with potentially devastating results.

1. To begin with, any relaxation of the attribution rule would render it virtually impossible for a defendant lawyer or law firm to obtain dismissal of a private securities-fraud action at the pleadings stage. In order to in-

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[2] Consistent with the rationale expressed in *Central Bank*, *Blue Chip Stamps*, and other cases, Congress has made the affirmative judgment that the elements of a private claim under Section 10(b) are capable of precise pleading and must be so pleaded on pain of dismissal. See 15 U.S.C. 78u-4(b)(1), (b)(2), (b)(3)(A).

[3] See *Merrill Lynch, Pierce, Fenner & Smith, Inc.* v. *Dabit*, 547 U.S. 71, 81 (2006) (noting Congress enacted securities litigation reform based on "policy considerations similar to those that supported the Court's decision in *Blue Chip Stamps*").

itiate such an action, plaintiffs' counsel would need only to identify some misstatement in a company's public filings and then to allege that the company's outside counsel participated in the drafting of the statement in question. Beyond that, plaintiffs' counsel would need at most to make factual allegations sufficient to associate outside counsel with the company in the mind of an "interested investor," see Pet. App. 24a—for example, by citing a reference to the identity of the advising law firm in the company's disclosures, or even by citing an article in the public domain noting that the law firm was representing the company. Such a complaint "is easy to craft and can be filed with little or no due diligence" on the part of plaintiffs' counsel. S. Rep. No. 104-98, *supra*, at 8.

As a practical matter, therefore, the only means by which a defendant lawyer or law firm will be able to obtain early dismissal of a private securities-fraud action is by invoking the heightened pleading standard for scienter. See 15 U.S.C. 78u-4(b)(2). In applying that standard, however, a court is required to take into account all of the allegations in the complaint. See *Tellabs, Inc.* v. *Makor Issues & Rights, Ltd.*, 551 U.S. 308, 322-323 (2007). And because securities lawyers frequently deal with complex legal questions based on incomplete factual information, see p. 6, *supra*, plaintiffs' counsel may be able to find some misstatement as to which, with hindsight, it could be argued that the lawyer or law firm was reckless in not noticing. Moreover, plaintiffs' counsel may be able to find other would-be defendants, including a company's officers, who have an incentive to point the finger at the lawyer or law firm and claim that they relied on their advice—even if the lawyer or law firm either never gave that advice or did so because they were themselves being misled by wrongdoers at the company. In any of those scenarios, it may be difficult, if not impossible, for a defendant lawyer or law firm to invoke the scienter requirement as a basis for dismissal.

2. If a defendant lawyer or law firm cannot obtain dismissal of a private securities-fraud action at the pleading stage, the ensuing discovery can be especially onerous. Plaintiffs' counsel understand that, in light of the fact that virtually all securities class actions are ultimately settled, it is likely that the defendants will ultimately bear both sides' litigation costs. See John C. Coffee, Jr., *Reforming the Securities Class Action: An Essay on Deterrence and Its Implementation*, 106 Colum. L. Rev. 1534, 1536 (2006). Accordingly, they have every incentive to "take up the time of a number of other people, with the right to do so representing an *in terrorem* increment of the settlement value." *Blue Chip Stamps*, 421 U.S. at 741. Indeed, securities litigation poses such dramatic discovery costs that Congress has imposed a mandatory stay on discovery in securities fraud cases until after the court decides the complaint states a claim. 15 U.S.C. 78u-4(b)(3)(B). The burdens of discovery are particularly heavy for law firms, because, unlike most businesses, the product that law firms primarily sell is the time of their people: *i.e.*, their lawyers and staff.

The securities litigation arising from the collapse of Enron presents a case study in the dangers of allowing a complaint to survive based on an amorphous theory of securities liability. Shortly after Enron's collapse, a district court allowed plaintiffs to proceed with claims against Vinson & Elkins (V&E) based on the theory, *inter alia*, that V&E had "draft[ed] and approv[ed]" many of Enron's disclosures. See *In re Enron Corp. Securities, Derivative & ERISA Litig.*, 235 F. Supp. 2d 549, 705 n.129 (S.D. Tex. 2002). In the ensuing five years of litigation, V&E produced more than 6.3 million pages of documents; thirteen V&E lawyers sat for 39 days of depositions and answered approximately 30,000 questions. Notably, that discovery occurred even though the court-appointed examiner in the Enron bankruptcy had concluded, shortly after discovery had begun, that V&E had not drafted Enron's disclosures; that V&E exercised no control over those disclosures; and that V&E's role in the preparation of those disclosures was in fact limited and episodic. See Enron Report, App. C, at 84, 87. Eventually, the plaintiffs voluntarily dismissed their claims against V&E, see *In re Enron Corp. Securities, Derivative & ERISA Litig.*, No. 4:01-cv-03624, 2007 WL 209923 (S.D. Tex. Jan. 24, 2007), but not before the firm had suffered substantial financial and reputational harm as a result of its involvement in the litigation. See Nate Raymond, *Vinson & Elkins Bolsters New York, Global Offices*, American Lawyer.com (Apr. 29, 2008) <tinyurl.com/v-enewyork>.

3. Like other classes of defendants, law firms will usually seek to settle securities litigation, even without regard to the merits of an underlying claim, in light of the financial and reputational harm from litigating a claim and the potentially astronomical damages in the event of a finding of liability. See, *e.g.*, *Stoneridge*, 552 U.S. at 163 (noting that the dynamics of private securities litigation "allow plaintiffs with weak claims to extort settlements from innocent companies").

Perhaps paradoxically, however, law firms are limited in their ability to settle claims, because they do not have the assets to pay large settlements without endangering their well-being. Cf. Ellen M. Ryan & Laura E. Simmons, Cornerstone Research, *Securities Class Action Settlements: 2009 Review & Analysis* 2 (2010) (noting that, in 2009, the average settlement in a securities class action was $37.2 million). Modern-day law firm partners are highly mobile and have limited incentives to remain with a firm that is about to pay a sizable settlement. See, *e.g.*, Terry Carter, *On the Hunt for Laterals*, A.B.A. J., Oct. 2006, at 27 (noting that "[l]ateral movement among law firms not only has lost its stigma, it has become a way of doing business" and that "[p]artnerships, in many instances, have become more contractual relationships than the traditional mix of personal and professional bonds").

Losing significant numbers of partners, in turn, not only can endanger the firm's ability to attract and retain clients; it can endanger the firm's access to lending facilities, a lifeline for many large law firms. One major law firm was recently forced to dissolve after a wave of partner departures breached a covenant in the firm's primary lending agreement. See News Release, Thelen LLP, *Thelen Management Recommends Dissolution* (Oct. 28, 2008) <tinyurl.com/thelenllpdissolution>. Put simply, every night, the major assets of a law firm pick up their briefcases and go home—and there is no guarantee they will return in the morning.

Indeed, that fate has befallen at least one major law firm already. In 2007, Jenkens & Gilchrist, at one point the largest law firm in Dallas, was driven into dissolution in the wake of a securities class action and investigation arising from the firm's involvement in the creation of tax shelters—work that had primarily been conducted by three lawyers in a branch office. The securities class action was settled in 2005 for $81.5 million. Although the firm likely would have survived the financial impact of the settlement itself, it was destroyed by the waves of departures that took place both before and after the settlement. Even plaintiffs' counsel acknowledged the unfairness of that outcome, stating that "99.9 percent of the people at Jenkens are good people and good lawyers" but that "[t]here were three bad apples[] and the bad apples upset the applecart in a big way." See Katie Fairbank & Terry Maxon, *How Jenkens & Gilchrist Lost Its Way*, Dallas Morning News, Apr. 1, 2007, at A1.

The current economic environment only exacerbates those pressures. The legal profession has suffered from an unprecedented downturn, with layoffs even at some of the Nation's most prestigious law firms. See, *e.g.*, Jeff Jeffrey, *Brutal Week May Not Be the End of Law Firm Layoffs*, Legal Times (Feb. 17, 2009) <tinyurl.com/brutalweek>. In fact, in 2009, more people were laid off by more law firms than had been reported in all previous years combined. See Kate Neville, *Law Firm Layoffs: Bad Sendoffs Can Be Bad for Business*, National Law Journal (May 28, 2010) <tinyurl.com/badsendoffs>. And this recession, like others, has precipitated an increase in litigation against law firms more generally. See Rachel M. Zahorsky, *Clients, Law Firms Get 'Savage' As Legal Malpractice Claims Increase*, A.B.A. J. Online (Feb. 17, 2009) <tinyurl.com/zahorsky>. With many law firms already at the tipping point, even the most meritless securities-fraud claim could be sufficient to push several over. The attribution rule serves as a vital source of protection against those claims.

4. Although lawyers and law firms would initially bear the brunt of liability under any more expansive standard for private securities-fraud actions, the eventual burden would fall on clients and the public at large. As Judge Boudin has explained, "[n]o one sophisticated about markets believes that multiplying liability is free of cost." *SEC* v. *Tambone*, 597 F.3d 436, 452 (1st Cir. 2010) (concurring opinion). The inevitable long-term effect of an expansion of primary liability for lawyers is an increase in the cost of legal services. Unlike a company and its officers, a lawyer typically does not benefit from

the success or failure of a securities offering; he receives the same hourly rate in either case. If the lawyer is liable for his client's statements, however, it will increase the risk of providing disclosure-related advice. The natural response will be to increase the "reward" for such advice, in the form of higher hourly rates. See Donald C. Langevoort, *Capping Damages for Open-Market Securities Fraud*, 38 Ariz. L. Rev. 639, 649 (1996). The increased cost of legal services will "in turn [be] incurred by the company's investors, the intended beneficiaries of the statute," *Central Bank*, 511 U.S. at 189, and "[t]he cost of capital will * * * increase just as if a wasteful tax had been imposed on capital formation," Joseph A. Grundfest, *Why Disimply?*, 108 Harv. L. Rev. 727, 732 (1995). In short, expanding liability for law firms under Section 10(b) will make the provision of legal services more expensive—and, as we will now explain, will also make it less effective.

D. A Rule That Permitted The Imposition Of Securities Liability On Lawyers And Law Firms Without Attribution Would Disrupt The Attorney-Client Relationship And Chill The Provision Of Legal Services

By placing substantial pressures on lawyers and law firms, a relaxation of the previously settled attribution rule would have deleterious consequences for the attorney-client relationship with no offsetting benefits.

1. Unlike an accountant, who "[b]y certifying the public reports that collectively depict a corporation's financial status * * * assumes a *public* responsibility transcending any employment relationship with the client," a lawyer is a client's "confidential adviser and advocate." *Arthur Young*, 465 U.S. at 817-818. Lawyers owes a duty of loyalty exclusively to their clients and must render advice consistent with their clients' interests. See Model Rules of Prof'l Conduct R. 1.13(a)-(b),

1.7 cmt. 1. Accordingly, in the ordinary course, lawyers are not permitted to disclose any information about their clients. See Model Rules of Prof'l Conduct R. 1.6(a). That is not to say that lawyers must ignore the interests of the public when advising clients. Lawyers must be aware of their clients' duties to the public, and, if a lawyer learns that a client is engaged in affirmative misconduct, the lawyer under certain circumstances can disclose confidential information. See Model Rules of Prof'l Conduct R. 1.6(b)(1)-(b)(3), 1.13(c).

Subject to those ethical obligations, however, lawyers are not "gatekeepers" of their clients and are not required to investigate their activities. In the wake of recent corporate scandals, the New York City Bar produced a report on whether lawyers should have a gatekeeper-like duty to the public. See Association of the Bar of the City of New York, *Report of the Task Force on the Lawyer's Role in Corporate Governance* (Nov. 2006) (New York City Bar Report) <tinyurl.com/barreport>. The report ultimately rejected the creation of such a duty, reasoning that "[r]ecognition of a duty to the investing public would represent a sea change in the ethical duties of lawyers and potentially in their relationships with clients." *Id.* at 61.

The American Bar Association (ABA) voiced similar skepticism about the creation of such a duty when it expressed its opposition to proposed rules implementing the Sarbanes-Oxley Act that would have done so. See Letter from Alfred P. Carlton, Jr., President, ABA, to the SEC (Apr. 2, 2003) <tinyurl.com/abaletter>. In response to those concerns, when the SEC promulgated its final rules, it decided not to require lawyers to "report out" of the company if they believe that a material violation of the securities laws or of fiduciary duties is reasonably likely, but instead to require them to "report up" within the corporate hierarchy. See 17 C.F.R. 205.3(b). In so doing, the SEC specifically recognized the professional and ethical obligations that lawyers have to their clients. See 17 C.F.R. 205.3(a).

2. Making lawyers liable for their clients' public statements would impose precisely such a gatekeeping duty and upset lawyers' professional and ethical obligations to their clients. Given the greatly increased risk that they would be defendants in securities litigation alleging misstatements in their clients' disclosures, lawyers would likely react in one of two ways. Some lawyers may be drawn to investigate their clients' disclosures, undertaking a process similar to that used by many law firms before issuing opinion letters in their own names. Other lawyers may take the opposite approach and refuse to investigate their clients' disclosures out of concern that any investigative action could be cited as evidence that they were aware of (or acted with reckless disregard for) the risk of misrepresentations in those disclosures.

In either case, the ability of lawyers to act as advisers to their clients would be seriously compromised, and the relationship of trust between lawyers and clients would be severely disrupted. In the former situation, clients may shield lawyers from information necessary for the lawyers to render effective advice, and the lawyers may be diverted from their primary responsibility of providing that advice. See, *e.g.*, New York City Bar Report 61-62 (noting that "clients would be more guarded in sharing information with their lawyers, and less inclined to include lawyers in meetings to discuss sensitive issues, if lawyers were viewed as having whistle-blowing duties to the investing public"). In the latter situation, lawyers may fail to learn the information necessary to render effective advice and, even where they do so, may fail to give the candid advice to which their clients are entitled. See Jill E. Fisch & Kenneth M. Rosen, *Is There A Role for Lawyers in Preventing Future Enrons?*, 48 Vill. L. Rev. 1097, 1128 (2003) (noting that "[t]he quality of the attorney's counsel is a function of the quality of information he receives from the client"). There is no valid justification for upending the attorney-client relationship in this fashion.

3. In fact, if lawyers are liable for their clients' public statements, it may have a chilling effect on the provision of legal services more generally. Law firms may not be willing to risk the increased exposure to securities litigation by representing newer or smaller companies, or companies on the verge of bankruptcy. And even with regard to more established companies, law firms may be leery of taking on representations during market downturns or fluctuations, which typically provoke spikes in securities litigation. For example, during the credit crisis of 2008, approximately 100 securities class actions were filed—the most since 2004. See Cornerstone Research, *Securities Class Action Filings, 2009: A Year in Review* 2-3 (2010). Ironically, it is precisely in those instances in which clients are in most need of expert advice from skilled counsel—but law firms are least likely to be willing to provide it.

When a lawyer is reluctant to provide candid advice to a client in need, the party harmed is not just the client; it is ultimately the public at large. This Court has explained that "sound legal advice or advocacy serves public ends." *Upjohn Co.* v. *United States*, 449 U.S. 383, 389 (1981). As the SEC has previously acknowledged, albeit in a different context, "[c]oncern about his own liability may alter the balance of [a lawyer's] judgment in one direction as surely as an unseemly obeisance to the wishes of his client can do so in the other" and that "neither is, in the end, truly in the public interest." *In re Carter*, Exchange Act Release No. 34-17597, 1981 WL 384414, at *25 (Feb. 28, 1981). As the SEC correctly concluded, a legal standard that "would permit a lawyer to avoid or reduce his liability simply by avoiding participation in the drafting process[] may well have the undesirable effect of reducing the quality of the disclosure by the many to protect against the defalcations of the few." *Id.* at *24. So too here, it would not be in the public interest for the Court to adopt a liability standard that chills the provision of legal services, and disrupts the attorney-client relationship, without any offsetting benefit.

4. Finally, a rule that permits the imposition of securities liability on lawyers and law firms without attribution is unnecessary to effectuate the remedial goals of the securities laws. As noted above, at the same time that it refused to create an express *private* right of action for aiding and abetting under Section 10(b), Congress expressly authorized the SEC to pursue civil enforcement actions on a theory of aiding and abetting liability for violations of the Securities Exchange Act. See p. 13, *supra*. The existence of those penalties serves as a strong deterrent for lawyers and law firms against participating in fraudulent conduct. As this Court has noted, moreover, the SEC "is not toothless" when it comes to exercising that enforcement authority. *Stoneridge*, 552 U.S. at 166. From 2002 to 2008, the SEC collected more than $10 billion in enforcement actions, see *ibid.*; earlier this year, the SEC collected $550 million from Goldman Sachs to settle one such action alone, see Final Judgment as to Defendant Goldman, Sachs & Co., *SEC* v. *Goldman, Sachs & Co.*, No. 10 Civ. 3229, Doc. No. 25 (July 20, 2009). The present regime also has the virtue of vesting enforcement authority in the SEC, which exercises discretion in commencing enforcement

actions, rather than plaintiffs' counsel. See *Tambone*, 597 F.3d at 452 (Boudin, J., concurring) (noting that "[t]he SEC may select its defendants sensibly; but private litigants have their own incentives"); Amanda M. Rose, *Reforming Securities Litigation Reform: Restructuring the Relationship Between Public & Private Enforcement of Rule 10b-5*, 108 Colum. L. Rev. 1301, 1338 (2008) ("The assumption that private enforcers are motivated by profit appears valid in the context of Rule 10b-5.").

Beyond civil penalties, moreover, lawyers and law firms face the risk of disciplinary sanctions for violating codes of professional ethics, which could result in their being deprived of their professions. And beyond even those sanctions, lawyers are largely selling their expertise and reputations—both of which would be called into question if a lawyer were found to have aided in a fraud. Even absent primary liability, therefore, lawyers already have ample incentive to conclude that aiding in a client's fraud is not in their self-interest.

As this Court has observed, "[e]xtending the 10b-5 cause of action * * * no doubt makes the civil remedy more far reaching, but it does not follow that the objectives of the statute are better served." *Central Bank*, 511 U.S. at 188. And that is particularly true where the practical effect of such an expansion would be to "expose a new class of defendants" to securities class actions. *Stoneridge*, 552 U.S. at 164. Extending liability to lawyers for mere participation in the preparation of statements ultimately made by clients would serve little purpose and would work great mischief. In deciding this case, therefore, the Court should make clear that lawyers, as outside service providers, cannot be liable for unattributed statements.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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