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THE SECURITIES AND EXCHANGE COMMISSION'S ENFORCEMENT PROGRAM: A DEBATE ON THE ENFORCEMENT PROCESS

MONROE H. FREEDMAN*
STANLEY SPORKIN**

I. OPENING REMARKS

MR. FREEDMAN: As you will hear, Stanley Sporkin and I have some fundamental disagreements with regard to policy. But Stanley Sporkin has, of course, earned the reputation as an unusually bright and dedicated public servant, and I'm genuinely honored to appear on a platform with him.

About six years ago I received an interesting proposal. That was, as a civil libertarian and somebody who had not been involved in securities regulation, to take a look at securities enforcement and react to it from a civil libertarian perspective.

I approached the subject also as a New Deal Democrat with considerable sympathy for the work of the Commission and, it's fair to say, some antipathy to what one SEC commissioner has referred to as "the robber barons, the princes of privilege and the malefactors of great wealth"¹—or, as Stanley Sporkin has put it, the Fat Cats, who are perhaps not entitled to quite so much sympathy as some of the people whom I had been working for as a civil liberties and civil rights lawyer.

What I found, however, is that the enforcement work of the Commission, at best, reflects an over-zealous insensitivity to individual liberties and the values of a free society; and, at worst, a deliberate pattern of serious and inexcusable violations of fundamental rights and elementary notions of fairness. Let me focus on four problem areas.

First—and one of the most serious abuses of the Commission in my view—is that it has sought to co-opt the private Bar into the service of the Government on behalf of government enforcement efforts. Private individuals are thus deprived of the zealous representation to which they are entitled under the Constitution and under traditional Anglo-American ideas of the attorney-client relationship and of professional ethics.

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¹ Garrett, *New Directions in Professional Responsibility, Address to the American Bar Association*, address by S.E.C. Chairman Ray Garrett, Jr., before the American Bar Ass'n, in Washington, D.C. (Oct. 11, 1973) [hereinafter cited as Garrett].

Second, the SEC has an inadequate program of training for investigating lawyers, and that has led to a variety of abuses which the Commission then justifies, when challenged, in a high-handed way.

Third, the SEC seriously abuses its power of obtaining publicity at pretrial stages to impose very severe punishment without due process and, after a consent decree, to give false and misleading impressions of the significance of particular consents.

And, fourth, the SEC has deliberately set out to chill freedom of speech by individuals by threatening to commence new or additional proceedings against those who criticize the Commission for the way in which a consent may have been obtained.

With regard to the co-option of the private Bar, the Commission asserts the best of motives. It says that it has a small staff, limited resources and onerous tasks to perform. Therefore the SEC states: "Members of this Commission has pointed out time and time again that the task of enforcing the securities law rests in overwhelming measure on the Bar's shoulders."²

That, to me, is a shocking proposition, that the SEC should require the private Bar to serve the purposes of government enforcement, rather than going back to Congress to request an adequate staff and budget to do its job. Instead, the Commission pressures private attorneys to serve the Commission, rather than their own clients. More than one commissioner has said that the private attorney's primary loyalty should not be to his or her client.

If there could be any question as to whether it is my position or the Commission's that is traditional, on the one hand, or radical, on the other, I would point to other quotes by esteemed members of the Commission. For example, former Commissioner Sommer has queried whether the SEC attorney is "another cop on the beat," and he has acknowledged that "all the verities and truisms about attorneys and their roles are in question and in jeopardy," characterizing the practices that the Commission is trying to induce as "revolutionary."³ Also, former Chairman Garrett has confessed to intimidating lawyers through what he has called "overly crude weapons," and he has explained that the Commission keeps the pressure on the private attorneys to do the government's job through a system of "suitable incentives," including both "rewards" and "punishments."⁴

The most vicious of the overly crude weapons, of course, is the 2(e) proceeding, under which the SEC claims the power to disbar or suspend the attorneys representing its adversaries under such extraordinarily

² In re Emanuel Fields, 2 SEC Docket 1, 4-5 n.20 (July 3, 1973).

³ Sommer, *Emerging Responsibilities of the Securities Lawyer*, N.Y.L.J., Jan. 30, 1974, at 4, col. 5, 6 [hereinafter cited as Sommer].

⁴ Garrett, *supra* note 1.

vague standards as that the adversary attorney is "lacking in character."

The ABA has used an illustration by analogy of two lawyers, adversaries to each other, each representing a company, and one of them having the power to disbar or suspend his adversary by going to the first lawyer's board of directors and having them pass judgment on whether the adversary has been overzealous or in some other way is "lacking in character."

When the lawyer no longer owes a primary responsibility to the client, we have not a double, but a triple conflict of interest; not just a conflict of interest between the client, on the one hand, and the Commission or the public interest on the other hand. There is actually, through 2(e) proceedings and other attacks directly against the private Bar itself, a triple conflict of interest, one in which the lawyer has to be at least as concerned with his or her own status and liability as with the client's or the public's interest.

With regard to abuses in investigation and lack of adequate training, I have obtained through the Freedom of Information Act access to the SEC's Enforcement Training Program Manual. It's a very hefty volume. I was interested to note, however, that there is nothing in it that advises those inexperienced young attorneys about the limits to which they can go in interviewing witnesses in preparing their cases. That has led, by way of illustration, to a case in which investigators went out and queried witnesses about a particular target. The witnesses found nothing improper in the way they had been treated by the target. Nevertheless, the investigators later came back, with a hard-sell approach that caused one of these witnesses to say—and this is an affidavit that he signed under oath and presented after consulting privately with his own attorney about doing so—that words had been put into his mouth through loaded and leading questions by SEC staff lawyers. The witness was also told in the second interview that although he had not found anything to complain of, the Commission had information showing that he had been cheated by the target, and that he should get even by cooperating with the SEC.

That affidavit and others submitted in the case were presented to a psychologist who has qualified innumerable times in judicial proceedings as an expert on memory, recall and testimony. He found the SEC interviewing techniques to be a clear example of "highly suggestive and biased interrogation," in which "the theory of the investigation was conveyed to the witness in a blatant manner," a manner which had been found by behavioral psychologists to produce "desired but inaccurate responses by planting false premises in the witness's mind."

When the issue was raised in Federal District Court through those affidavits, I wondered how the SEC would respond. Although I fully believed our affiant, I half-expected that the SEC might come back with affidavits from its own investigators saying that they had never done

any such thing, and presenting training material showing that such tactics would be contrary to established SEC practice. On the contrary, however, they made one argument, and one argument only, to the Federal Court. That is, that the SEC is entitled to investigate cases in any way it sees fit.

With regard to publicity, authorities have noted the "cataclysmic effect"⁵ of pretrial publicity, "more severe than any penalty the Commission could properly impose for the alleged violation."⁶ The SEC's response, of course, is that they feel an obligation to alert investors and to inform the public.

Isn't that a Wonderland approach to justice? Punishment first—indeed, a cataclysmic punishment—punishment first, and trial afterwards.

I have seen that applied in a case, for example, where the alleged misconduct had ended five years before, and in which we were about to have a hearing, so that within a very short time, if the Commission prevailed, they could publicize the case after proving the respondent guilty. Although under no theory were investors in urgent need of warnings, the SEC was insisting upon smearing the respondent's name before he had even had his day in court.

After a consent is obtained, the Commission insists upon its asserted right to publish the consent, along with the allegations of the complaint, in a way that creates a false and misleading impression of what has been consented to. At the same time that the Commission is so eager to exercise its own power of publicity, however, the Commission has chilled free speech on the part of individuals.

Chairman Williams has announced on more than one occasion that when an individual enters into a consent decree with the Commission, that individual is thereafter forbidden to discuss that consent or related enforcement policies. The reason given is one with which Richard Nixon and others would find great sympathy—that exercise of such speech creates a false impression of our enforcement program.

That is the classic tyrannous argument against free speech—that it creates a false impression about what public officials are doing. In order to achieve that chilling effect, the Commission has expressly threatened to re-open consents or to start new proceedings against the individual who chooses to speak.

That, of course, stands the Constitution on its head. The government insists on speaking all it wants, even if that means smearing somebody's name before trial or giving a false or misleading impression of what a consent was. Yet the government seeks to deny the individual the right to say, for example, "Yes, we consented, and one compelling reason for

⁵ See Gellhorn, *Adverse Publicity by Administrative Agencies*, 86 HARV. L. REV. 1380, 1394-98 (1973).

⁶ SECURITIES AND EXCHANGE COMM'N, REPORT OF THE ADVISORY COMMITTEE ON ENFORCEMENT POLICIES AND PRACTICES 20 (1972).

the consent was the enormous expense of trying this case and the time that it would have taken out of our regular business and our ability to earn a livelihood"—reasons that every lawyer will tell you are major factors, if not paramount, in decisions to consent. Thus, the Commission insists upon its right to speak out, and yet would deny individuals their First Amendment rights.

Let me close with a hypothetical situation suggested by Carl Schneider of the Philadelphia bar. I would be interested in having Mr. Sporkin's evaluation of it. Let us say you are a lawyer representing a company that is preparing a prospectus. There are some very delicate issues of disclosure. The disclosure statement as drafted is unquestionably adequate. However, the company is concerned about a sentence suggesting that there might have been Robinson-Patman Act violations on the company's part. They want to know whether that can be omitted or at least modified in a significant way.

You make a professional judgment in two parts. First, there is a strong likelihood, although not a certainty, that the Commission would consider it inadequate. Second, if the Commission were to challenge your client on this as a failure to disclose, you've got about a 50-50 chance of persuading a court that there is no violation. You tell that to your client. Your client then makes the business judgment that they are prepared to take the risk, and that they prefer to delete the particular disclosure.

Is the lawyer in any jeopardy whatsoever if the lawyer does not take that issue to the Board of Directors and/or to the SEC?

MR. SPORKIN: I think it is important to air our differences when people come forth like Monroe and criticize some of the processes of the SEC. I am glad to see tonight that Monroe does not question the need for the Commission as he has in the past. I would like to make it clear that I believe that the Commission has proved itself to be a necessary institution of our government and that it plays a vital role in carrying out its mandate of protecting investors. We at the Commission are quite proud of the agency, as it has remained faithful to its mission over the years. This has not been an easy task for a government agency as you know.

There has been tremendous criticism over the years at agencies which stay in business for a period of time. They sometimes are co-opted by the people they regulate. I'm proud to say that that hasn't happened to the SEC. Indeed, if you look at the record of the SEC in this era of rating agencies, I think you'll find that several years ago that the Congress of the United States gave us a number one rating.

Well, maybe I would not be such an easy grader. In terms of what we would now deem the era of the 10's and 11's, I think we probably rate perhaps an 8, 8½. And I think, by and large, those who deal with us would agree that the Commission is doing a pretty reasonable job.

Now what you've got to realize is that it often becomes very difficult for the Commission to carry out its enforcement role because—as other

government agencies have experienced—we never have all the resources that we need. Nevertheless, we try to do the best that we can.

Contrary to what Monroe has said, we do not try to conscript the Bar to do our work for us. What we try to do—is to ensure that the attorneys, accountants and others who provide offerings with access to the marketplace are held strictly accountable for their own participation in such unlawful activities. This is what has become known as the access theory.

The access theory is very simple, and it's one which nobody should misunderstand. It says, in effect, that lawyers do not have any immunity; when they participate in a crime they're going to be treated like other law violators. This issue is totally separate from the issues dealing with legal representation of those under investigation. Lawyers understand that they are obligated not to involve themselves in the dishonesty of their clients. If they do, they're going to have to pay whatever price they have to pay.

Monroe's affidavit story almost reminds me of the famous senator who used to say I have here an affidavit that says so-and-so-and-so-and-so and therefore it must be true. Well; I think Monroe knows that's only one side of the story.

You must realize that here we have an agency, a law enforcement agency. That all we have as a tool of our enterprise is the ability to issue process. I must tell you that our people are well trained. They are told to be fair, they are told to be decent people. We don't engage in the wiretapping that has brought other agencies under criticism. We don't have black bag jobs. We don't invade psychiatrists' offices. We don't do any of those kinds of things that other agencies have been criticized for. The only thing that I've heard here today is that some psychologist has stated that the way we asked a witness a question in an investigation somehow misled that witness.

But believe me, as Monroe knows, that gets tested in court. And all that information can be brought up in cross-examination, which I'm sure he does as an experienced trial lawyer and which everybody else would do.

So what we've got to do is to put things like that aside. Obviously we don't want our people to do things other than treat people honestly and fairly, but you don't condemn a system on the possibility that one lawyer went out and asked a question in a way with which Mr. Freedman disagrees. I would have loved to have seen the questions Mr. Freedman would ask in preparing a witness for questioning.

Now with respect to the business of co-opting the Bar, I think that with so many able people in this Bar, I think it really is an affront to the members of the Bar to suggest that the Commission would first of all, be able to co-opt them. Secondly, it is an affront to members of the Bar to say that they would agree to such a process. I think you've got to realize that just because a lawyer believes it's in the best interests of his client

to try to get his client out of problems and to settle the case with the SEC doesn't mean that he somehow is not a good lawyer. You don't have to be a macho lawyer in everything you do in order to be a good lawyer. The most effective lawyers that I've seen are those lawyers who can deal with a client's problems, resolve those problems and get their client on to doing his or her everyday business.

The most ineffective lawyers I've seen, although again it's their right to do so, are those lawyers who will go in and contest the Commission on every procedural issue. They'll contest, for example, the issuance of the order. They'll contest whether it's a private or public proceeding. They'll contest whether the Administrative Law Judge listened to this person or listened to that person.

They'll contest all the procedural issues, never wanting to get to the substance. And then when they lose the procedural issues, they have expended everything they have and they're not prepared to try the case. And so what they do is consent. I don't think that is very effective representation of a client.

As everyone knows, legal representation in these cases is a very expensive proposition. Monroe has said that clients agree to consent decrees because they cannot afford to defend themselves. Well, that is not a problem endemic to the SEC. It is a problem with society in general today and it is a problem of the legal profession. I, too, am very disturbed by the fact that legal fees have gone sky high. But don't saddle the SEC with that burden. We can't do anything about it. We have the same problems as everybody else. The problem is that the cost of all litigation is extraordinarily high.

The publicity issue was first raised by a person with Monroe's namesake, Milton Friedman, back in 1967. But we're talking about 1980. How in this day and age should we talk about private proceedings as being appropriate? How in this day and age, when we're talking in terms of openness of government, are we going to talk about a closed proceeding?

Pretrial publicity is a question of jury prejudice in a criminal case. Here we don't have a jury, it's an administrative proceeding with a sophisticated judge. To try and turn the clock back twenty or thirty years by requiring a closed process would obviate all the advances of open government.

What is more disturbing is that Monroe Freedman, of all people, should be urging return to private government. Now with respect to Chairman Williams and the Commission's view concerning persons who walk away from a consent decree once they agree to it; I think that you've got to understand what underlies the Commission's position.

What the Commission is concerned about is the same thing that the criminal courts are concerned about. A criminal court judge should not take a plea from a defendant if that defendant denies that he committed the act. It's wrong.

The Commission has said very simply that when you sign a consent.

decree that says that the defendant does not admit or deny that he committed the act, you shouldn't go out tomorrow and deny committing that act. Tell us up front because if you didn't do the act then we ought to litigate.

It is a fairness issue and the sense of what we're saying is that if you want to go and deny any violation then we feel that you've broken faith with your statement. You have misrepresented your position to us, and therefore we in effect state: "Fine, let's reopen the case and let's have a trial to determine the facts."

That's all we're saying. Now if that is being unfair, if that is being wrong, then I guess we've got to plead guilty to being wrong and unfair, but I don't think it is. To the contrary, I think it's being eminently fair in conducting public business. A person should not be able to consent if he denies.

One point I would like to make is that while we are focusing on the SEC in this debate, we should remember that some members of the bar have at times engaged in questionable practices. Think about the lawyers we have seen who withheld documents improperly. Think about the lawyers we have seen who have taken side deals and not told their clients of the commissions and other benefits that they've accepted to the detriment of their clients. Think about the lawyers who, over the years, have worked to keep a deleterious product on the market through the exercise of procedural maneuvers that can be utilized by any attorney in the United States.

The point I am making is that we do not condemn the entire Bar for these individual acts. Similarly, we cannot condemn the entire Commission for some over-zealous individuals. The kind of case that has been made here today is the kind of case that I could argue to the court without putting on a witness. Monroe has not made a claim upon which relief can or should be granted.

Finally, I will now try to deal with Mr. Freedman's hypothetical. Because the hypothetical had so many if's, and's and but's about it, it becomes very difficult to follow. I must change his hypothetical a little bit, in order to deal with it. In other words if there's a question whether it could or could not be a violation, it is difficult to answer.

Let us assume that there is a known violation of the Robinson-Patman Act and it is clear that the possible consequences are quite material on a financial basis. I submit to you that a company that goes to the marketplace knowing that information without disclosing it has violated the law. If an attorney puts his name on that statement with that knowledge, he in effect endorses and adopts that statement. In that case I would say to you that it's highly likely that the attorney himself is in difficulty.

The last thing I will mention concerns the 2(e) power of the Commission. Since I am sure that there will be a lot of questions on it later, the only thing I will say is that the Second Circuit—the latest court to hear

the issue—has upheld the power of the Commission to bring 2(e) proceedings.⁷

II. QUESTIONS AND ANSWERS

Question: We've been talking, in part at least, about consent decrees. One of the lawyer's obligations, in advising his client as to whether to settle a proceeding or settle an action, is that he must do it on the basis of informed consent. In my experience it is sometimes difficult for the lawyer to advise his client, to have him consent in an informed manner because he can't get information as to what the case, the factual case, is against his particular client. He cannot get copies of transcripts of other witnesses who may have testified in an investigatory proceeding or other evidence that may be the basis of the staff's case.

Mr. Sporkin, would you care to comment on that?

MR. SPORKIN: Obviously it depends on what time the consent comes in. If it comes in at a time when the case has been filed, there's no problem. What you're talking about is a situation where in the investigative stage, the lawyer comes forward and says, "Look, if we've done something wrong and we believe we probably have, we'd like to consent but, you know, we'd like to see what this thing is all about."

That's the same problem I guess a prosecutor has. Generally speaking, the practice at the Commission is to sit down and go over the facts with counsel when it is not going to compromise the case. Actually showing counsel the transcripts, however, is a very difficult situation because there's a problem of our ability to show you somebody else's transcript. I don't think it would be fair to that person. But you always have the right to see the document that you're going to consent to, whether it be a complaint or a 2(e) proceeding, and that document generally will contain the specific allegations.

I don't know what else to tell you other than if you're doing a good job, you should insist on knowing what the facts are and what your client is alleged to have done. Otherwise I don't think you can in good conscience advise your client to consent.

QUESTION: This is a question for Mr. Sporkin. Earlier you were commenting on your ability to bring enforcement proceedings against lawyers and the example you used were those lawyers and those accountants who provide access to the marketplace for public companies.

Do you mean by using that example that you do not have the ability to bring enforcement proceedings against lawyers who are engaged in defending corporations in enforcement actions? Are there situations where you might be bringing enforcement proceedings against those lawyers who are strictly defenders of others?

MR. SPORKIN: I think you make a good point there. The vast

⁷ See *Touche Ross and Co. v. S.E.C.*, 609 F.2d 570, 582 (2d Cir. 1979).

majority of disciplinary cases that we have brought have been against lawyers acting as counselors or advisers.

I don't think the latter case poses the kind of problem that Monroe was talking about.

As a tribunal, the Commission has to be able to deal with obstreperous or contumacious conduct before it. Indeed, as I read the critics of the 2(e) process, the one area where they believe that they would concede that the SEC has authority is when there is contumacious conduct before the tribunal.

My answer to you is I don't know of any case that we have brought which involves a lawyer in his adversary role. There have been instances where conduct has been so contumacious that consideration was given to a disciplinary proceeding. For example, there is one instance I recall of an attorney who allegedly lied to a staff member in a settlement discussion. However, in this particular case no action was taken.

MR. FREEDMAN: I would like to comment on that. I think it is a fallacious distinction between the lawyer who is serving as counselor or adviser to the client and the lawyer who is representing the client in actual litigation. Potentially, there is always an adversary aspect lurking in any relationship of this kind; whether we are talking about two partners who want amicably to form a partnership or begin a business venture or two people who are in love and are going to get married. Whatever it may be, there is always a potential for something to go wrong. One of the lawyer's jobs is to think beyond where the clients are thinking at the moment.

The most serious of these potential adversary situations, and in which we all know as a matter of fact the adversary relationship begins not some time later on, but right now, is between the Securities and Exchange Commission and somebody who is subject to its jurisdiction.

No lawyer waltzes in thinking, "We are dealing with our good friends, the SEC, and everything is going to be friendly." I think the very hedge that Stanley gave in answer to the question I posed is a good indication of what the problem is. He has left, at the very least, a very substantial chilling effect on the lawyer who gives his or her best professional advice in good conscience and, as I understand it, is going to be in jeopardy for not turning the client in to the SEC.

There was a qualification he made to the question, which I should have added. That is, you have a case where the SEC is likely to disapprove, the court's decision is about 50-50, and then add that the company subsequently is charged and found guilty of a violation. Is the lawyer in jeopardy? And if the answer is yes, the lawyer is in jeopardy for having given conscientious legal advice, and not compelling the client to make a particular business judgment on that advice.

I think that's outrageous, and I know that it is, as it has been characterized, making the lawyer "another cop on the beat;" making the lawyer the "adversary" of his or her client. When does that adversary

relationship begin? It begins, apparently when the client walks into the lawyer's office and says, "I'd like you to help me with a registration statement." The adversary relationship begins then, between the lawyer and the client.

I think it is disingenuous for Stanley to say that nobody in this room has been co-opted. Of course nobody will stand up and admit to having been intimidated. Yet how does one explain the quoted statements that I have given you about "overly crude weapons" of "rewards" and "punishments" to keep the lawyers in line? And, "Members of this Commission have pointed out time and time again that the task of enforcing the securities laws rests in overwhelming measure on the Bar's shoulders."

Now, Stanley can say that doesn't mean co-opting the services of the private Bar for enforcement, but those words are about as plain and simple and direct as you will ever get from the Securities and Exchange Commission on any issue.

Turning to Stanley's version of my hypothetical, we're talking about a situation in which it's clear the client is in very serious jeopardy and the client is going to get caught. What you want to do is, again, co-opt the lawyer into the services of the Government in helping to punish the client.

That's where I draw the line. I'm not in favor of false statements; I'm not in favor of fraudulent offerings; what I am against is policing that kind of conduct by using the private Bar. It's a question of the methods of enforcement that I'm objecting to, not whether wrongs should be corrected and enforced.

MR. SPORKIN: I still don't know the answer to the question. As a lawyer, do you walk away, or do you continue to process? You've got to pull the delaying amendment to get it effective. Do you do it, or what do you do? I've got to get an answer to that.

MR. FREEDMAN: I thought I had given the answer. The answer is that the lawyer should not knowingly proceed with a false statement or fraudulent offering, unless by withdrawing at that point the lawyer would directly or indirectly be divulging a confidence of the client. If the lawyer would be doing that, then the lawyer's job is to go forward.

One of the elements, therefore, is the policy of the government agency when the lawyer withdraws. If the agency is going to treat that as a red flag, thereby creating a situation in which the fact of withdrawal is tantamount to disclosure to the Government that the lawyer thinks something wrong is going on, then it is the lawyer's obligation not to withdraw at that point.

MR. SPORKIN: I tell you, if that's the test then you're putting the test on the private person, which makes it a very difficult test to apply.

Suppose that the examiner on the case had asked you four weeks before if there were any problems, and you had honestly represented that you didn't know of any and you had written and signed a letter over

your signature that said, "We have no antitrust problems." Then at the last minute the examiner says: "Now is everything you've told me in the past, Mr. Freedman, true as of today? Because your representations will speak as of the time we lift that delaying amendment."

MR. FREEDMAN: One of the problems between us is that you are arguing, in effect, that what exists as policy and practice is right. And I am challenging that system. I am challenging a system in which, for practical purposes, you have to have a lawyer who is going to know your business, and for practical purposes that lawyer is put in the position of having to answer questions to the Government about what is going on. That is the fundamental impropriety.

For an examiner to ask a lawyer about the lawyer's client's business, rather than asking the client himself, is one of the wrongs about which I am complaining.

You succeed in setting up a system in which the lawyer knows and is asked, rather than asking the client. And then you say: We have put the lawyer in a position where the lawyer has said something that the lawyer thought was true and now knows isn't true. What should the lawyer do? The answer, is, the lawyer shouldn't have been in that position in the first place. I think the system is inconsistent with our fundamental notions of liberty and of private autonomy when it functions in that way.

MR. SPORKIN: But, Monroe, you've got to understand that the lawyers are holding themselves out as providing advice. As an aside, I don't know whether I disagree too much with you when you say that a lawyer ought not to get in that position. Then people filing registration statements ought not to use lawyers. Now we can deal with that.

The reason the SEC gets into this position is because it's the client that's interposing the lawyer between itself and the Commission. There's no law that says you've got to use a lawyer, then the lawyer cannot be what I consider to be a person that's going to ask no questions, see no evil, do no evil, hear no evil, and just go forth blindly and do his client's bidding. I think it has got to be more than that.

MR. FREEDMAN: There's no law that says that you have to have a lawyer represent you in a criminal matter, yet people have lawyers represent them in criminal matters.

MR. SPORKIN: The Constitution says that.

MR. FREEDMAN: No; it says you have a *right* to counsel. It doesn't say you *must* have counsel. As a matter of fact, you have a constitutional right *not* to have a lawyer if you don't want to.⁸ The Supreme Court held that, too. It's the same Supreme Court that held in the

⁸ See *Faretta v. California*, 422 U.S. 806, 836 (1975) (sixth amendment as made binding on the states by fourteenth amendment, guarantees defendant in state criminal trial an independent constitutional right of self-representation).

*Alford*⁹ case that you can protest your innocence and still enter a guilty plea. The Supreme Court recognized, because of the risks, expense and embarrassment of defending case, that the law in its majestic equality will permit the innocent as well as the guilty to plead guilty and get the benefits of plea bargaining.

So the gentleman in the rear was correct, Stanley: you're simply wrong on the law. A common criminal can protest his or her innocence and, at the same time, plead guilty. That carries the imprimatur of the Supreme Court.

You can go to jail for it, and shout out the jailhouse window, "I am innocent," and that is protected by the First Amendment.

MR. SPORKIN: Then I don't understand why the courts in the United States go through such an elaborate procedure when a defendant comes up and wants to enter a guilty plea. The court asks: "Did you do it?" and the person says they didn't do it. And I've seen courts say, "I'm not going to accept that plea."

MR. FREEDMAN: Since *Alford*, they're not required to do that. They're to ascertain whether there is a factual basis for the plea, even though the defendant is insisting upon his or her innocence. The court need only satisfy itself that the defendant is right in being concerned about the risk, expense and embarrassment of defending him or herself, even though innocent.

QUESTION: This is a question for Mr. Freedman. I'm interested in your comments about the abuses by the Commission staff in investigations. I'd like to separate out actual abuses—which I don't think anyone in the room would condone, even as you posit them—from a discussion of the overall process. And I'd like to hear from you, in your position as a critic of the Commission's investigative process, what safeguards you would think the Commission ought to afford persons in investigations other than the following: the Fifth Amendment warning; the right to the charges in a formal order; the right to a transcript; warnings about privacy; warnings about the FOIA; warnings about the Trade Secrets Act; warnings about the opportunity to put in a Wells Committee submission, which contains both facts and law; the opportunity to speak not only to the staff attorney responsible for the case, who may be a new staff attorney, but a number of supervisors all the way up to the Commission; the opportunity at any time to take a matter directly to the Commission, and, the opportunity to go to court and challenge the investigative process. And also the ultimate opportunity, the opportunity to contest the charges in case an action is instituted; the opportunity to review a complaint in the context of a settlement discussion; the opportunity to review a press release in the settled context; the opportunity to negotiate language in the settlement. Besides the ones just listed,

⁹ North Carolina v. *Alford*, 400 U.S. 25, 37-38 (1970).

what other safeguards in the process—and putting aside the abuses, which I can't accept, either—do you think ought to be available in a law enforcement agency, and suggest to me any other law enforcement institution which affords such safeguards to the people.

MR. FREEDMAN: Well, your question assumes that certain things are given as a matter of right. Not all of those things are given as a matter of right. For example, the Wells submission: unless that has happened very recently and I missed it, there is no such right. Is there, or isn't there?

QUESTION: When you use "right" do you mean *de facto* right? I don't think there's any case except maybe one out of a thousand in a situation where, because of the exigencies of time, the Commission determines that it has to move without the opportunity for a submission. And we've drawn the distinction between "right" as a matter of law and "right" as a matter of fact, simply to preserve to the Commission that very minute opportunity, or very rare opportunity, when time has not permitted because of an on-going situation.

I question whether or not any plaintiff—even if the SEC as a plaintiff—is required to identify charges to a defendant before he sues.

MR. FREEDMAN: An *ex parte* hearing, before the body that is doing the judging at an important stage in the proceeding, is offensive to due process.

One of the things that I did notice in the SEC Training Manual—which had no advice at all to young and inexperienced lawyers about the proprieties and the limits on investigating cases—was the instruction to the staff attorney to be sure to be present when the Commission takes up your case, even though, of course, your adversary is not going to be there. Even if you have a Wells submission, your adversary is not going to be there, is not going to have the oral access to the Commission that is urged upon the staff attorney.

But if what you say is true, and if the denials of due process are only sometimes, and not most of the time, why can't the Commission issue a rule that makes an exception for the exigent case that you mentioned? Rules like that are drafted all the time.

It is a suspect situation at best. One is led to wonder—by quotes that I have not made up, but which have been published, regarding rewards and punishments—whether the privilege of making a Wells submission is one of the areas of reward and punishment. If you are in the Commission's favor, you get the opportunity, if you're not, you don't.

And if that inference is wrong, why over the years—with people as prestigious as Milton Friedman and Manny Cohen recommending it—why is it the Commission has not been willing to state its policy in so many words?

QUESTION: I could answer that, but I would like to know: besides that issue, is there anything else?

MR. FREEDMAN: Yes. People who are targets being called in and

not knowing that they're targets; people finding out for the first time in the newspapers that charges have been brought against them, at the same time that their friends and neighbors and business associates and people they want to do business with find out about it.

QUESTION: Could I ask you about the latter one? Do you think there's an obligation on the government, as a plaintiff in a civil injunctive action, to call up the defendant; and an obligation, as opposed to whether or not as a matter of courtesy it ought to be done? And it is done, in almost every case. Do you think that it's an obligation, that it should be a requirement?

MR. FREEDMAN: I'm talking about fundamental fairness.

QUESTION: As a matter of fundamental fairness, do you think that it's required?

MR. FREEDMAN: Yes, I'm talking about a situation in which every single commentator has noted that publicity will have, ordinarily, a far greater impact than any penalty that the Commission has been permitted by Congress to impose.

There's an important distinction to make. Stanley fudged it when he was talking, when he referred to the Star Chamber. I am not saying that all hearings necessarily should be closed. There's a difference between saying that hearings should be open and, at the same time, saying that the government should not be able to destroy someone's reputation through publicity without due process and without giving that person a day in court. There is no reason to issue press releases, replete with charges against people who are in a very delicate professional position, when you know as well as I do, the very release of those charges is going to have a penalizing effect.

QUESTION: Do you think it goes the other way, just to finish it off? When I am sued by someone whom I'm investigating, do you think I should be called by the lawyer who's representing that client and be advised in advance that I'm going to be sued?

MR. FREEDMAN: We're talking about the obligations of the Government. That's another indication of a lack of sensitivity on the part of the Commission as to what the Bill of Rights is about.

The Bill of Rights does not give rights to the Government; it gives them to the people, to individuals, to citizens, to persons. It's persons who have rights such as free speech. As I pointed out, the Commission insists upon its right to publicize, and yet will chill the right of individuals, persons, to their free speech.

QUESTION: So therefore when I'm sued as an individual I don't have the rights, only because I work for the Government? That is the logical conclusion to what you said.

MR. FREEDMAN: If you are sued by a private party, you do not have the same rights as if you are sued by the Government; yes, that certainly is true. If I am sued by a private party, I do not have the same rights as I would if sued by the Government.

MR. SPORKIN: You know, Monroe, you throw these terms around, like "rights." But I gather you're the one who's determining these rights.

Take a criminal case, for example. Every day you see in the press that the government has issued an indictment against somebody. Are you quarreling with that practice? Do you say that violates constitutional rights? If it does, then those rights have been violated for many, many, many years.

MR. FREEDMAN: I agree with you.

I have shared a platform with Maurice Nadjari and before a large audience of the New York Bar. I would say there was virtual unanimity in that audience with the proposition that I stated, that Mr. Nadjari was committing serious violations of professional responsibility as a prosecutor, and violating people's constitutional rights, by holding press conferences and by issuing press releases detailing the allegations of complaints.

MR. SPORKIN: You're going further than that. Are you saying that the government can issue a press release, but not the kind of press release that discusses the charges?

I was reading an article today about the Son of Sam. I hope we haven't forgotten about him. Are you saying that the government is depriving the Son of Sam of his rights when they put out a press release indicating that they were able to apprehend the Son of Sam, and stating that he's been charged with murder? Is that violating Son of Sam's rights? Is that what you're suggesting to me?

MR. FREEDMAN: I am suggesting that Government fulfills all of its obligations to the people, and does not yet cross the line of infringing on the rights of the accused, by putting on the public record the charges against him and by arraigning him in open court. It is not necessary to issue any press releases, to hold any press conferences, or in any other way to prejudice a fair trial and harm an individual's reputation.

MR. SPORKIN: Well then, say you don't tell the press, but the press can come down to the courthouse and they pick up the charges, and they can write them; is that correct?

MR. FREEDMAN: That's absolutely right, yes.

MR. SPORKIN: What is the difference? I don't understand.

MR. FREEDMAN: I think there's an important difference, Stanley.

MR. SPORKIN: What?

MR. FREEDMAN: And I think that if you didn't see the difference, you wouldn't go to the expense of issuing the releases.

MR. SPORKIN: I think an agency has the duty and responsibility to be able to put out press releases in a business-like fashion and to account for what it does.

MR. FREEDMAN: You can account for what you've done after the case is won; you don't have to do it before.

MR. SPORKIN: You know as well as I do that all you're doing is setting up again the kinds of procedures that make it impossible for the public to be protected.

Remember the public has some rights too here: the public has the right to be informed and to know what's happening.

Now all you're saying is the press has got to be more diligent. As I understand it, if a prosecutor says, "We have filed an action against the Son of Sam and we've charged him with murder one in five instances," that somehow that violates the Son of Sam's rights according to you. But if the prosecutor has put in an indictment and the press comes along, gets the indictment and prints it, then somehow the Son of Sam's rights have not been violated.

MR. FREEDMAN: You've picked a very cute case. You've picked a case that was so notorious that any reporter would have that information from the public record anyway. But we're talking about the run of cases where the Wall Street Journal or Barrons or the New York Times would not even know about it, except for the fact that they rely on your releases. And I suggest that's precisely why you spend the public's money to print and publish those releases.

MR. SPORKIN: So what you're really saying to me is that we ought to have two kinds of standards, one for the Son of Sam and the other for all other kinds of people? The Government ought to grade people.

And it can put out a release with respect to those that it believes are serious violators. But with respect to those that it believes maybe have just had a parking ticket, then it ought not to put out a release. Is that what you're saying?

MR. FREEDMAN: No. I said the standards should be the same. I stated very clearly, the Government has exhausted what it can and should do by way of avoiding Star Chamber or secret indictments when it puts the indictment on the public record, when it goes through the ordinary criminal processes of arraignment and presentation and so on.

MR. SPORKIN: Do you think in your lifetime that you're going to see the Supreme Court or anybody else saying that you violate somebody's rights for the government to put out a press release?

MR. FREEDMAN: I'm suggesting to you, Stanley, that the standard of what you can get by with, in terms of hurting people before you try them, should not be the standard of somebody with Stanley Sporkin's reputation, and the kind of conduct you yourself demand from others.

When you say, "Do you think the courts are ever going to slap us down? I can get away with it," I don't find that satisfactory coming from you.

MR. SPORKIN: But, Monroe, you know when you talk about fundamental rights, I believe that I am protecting the public and that the public has fundamental rights. I'm bothered, quite frankly, when I see

some of the things that you have put out, particularly when they defy what I believe to be honesty and integrity.

Let me just read for you, for example, now that you've adopted this code that you are reporting on, how you suggest that lawyers should conduct themselves. This is what bothers me because what you're doing is trying to turn common sense and good judgment on its head. If you do that, then you've done away with realism and nothing can operate properly.

For example, you have an example in your American Lawyer's Code of Conduct of a lawyer who learns from his client during the trial that the client intends to give testimony that the lawyer knows to be false. The lawyer does not present that client's testimony as he otherwise would, but instead simply requests a narrative from the client and returns to his seat at the counsel table. On summation to the jury the lawyer makes no reference to his client's testimony contrary to what he would have done he had not known it to be false. Under your code, the lawyer has committed disciplinary violations both in the manner of presenting the client's testimony and in the manner of the summation.¹⁰

Now I must tell you that this is so bothersome to me because it is totally inconsistent with what I consider to be fairness, fundamental rights and decency. I can't believe that you would have a lawyer that would ever be disciplined for doing what that attorney did in this case. I can't believe that you could do something like that. He might as well go out and bribe a juror. If he did bribe the jury and told you, could you disclose it?

MR. FREEDMAN: Stanley, should I read you the provision? In fact it says that a lawyer need not knowingly proceed before a corrupted judge or juror even if it involves disclosing a confidence. You know, it's easy to pick out one section of context.

MR. SPORKIN: What's the whole context here?

MR. FREEDMAN: For example, you have suggested that the section means bribery is all right, and you're wrong. That's part of the context you took it out of. You're suggesting that as long as a lawyer hasn't done the bribery, it's all right. You're wrong. You took it out of that context.

MR. SPORKIN: We're making progress.

MR. FREEDMAN: In addition, that particular position that you criticized has been endorsed by a number of Bar associations and reflects the practice in the District of Columbia of about ninety percent of the practicing Bar according to a confidential survey that I had nothing to do with.

MR. SPORKIN: You have found an attorney that has been disciplined for doing what this lawyer did in this case? If that is so, then I

¹⁰ THE AMERICAN LAWYER'S CODE OF CONDUCT 109, illus. case 1(i) (public discussion draft, June 1980). See also *id.* 1(j) & 605-06, illus. case 6(a)-(d).

believe that many of us in this room will have to give up the right to practice. I really believe that. It is so offensive to me to think that I have a duty when I know that somebody has lied to argue to the jury that the false evidence is true when I know it's based on lies.

MR. FREEDMAN: Wrong. You don't argue that. Under the present code of conduct, you are forbidden to vouch for your client's case. You don't argue it is true. You argue that it is evidence in the case, and that's the way that illustration is worded.

MR. SPORKIN: You argue as if it is evidence in the case, the way I read it.

MR. FREEDMAN: Yes, you do.

MR. SPORKIN: So, therefore, if the person said, "I did not shoot the gun on a certain night," you argue that the person said, "I did not shoot the gun."

MR. FREEDMAN: You include in your marshalling of facts the testimony of the defendant that he or she did not do it. That's exactly right.

MR. SPORKIN: I can't buy it. Tonight I'm not buying it.

QUESTION: This is for Mr. Freedman. You mentioned just recently that a lawyer has the duty not to vouch for false statements by his client. In a situation where a lawyer is putting together a prospectus and silence could be construed as a false statement, does not the lawyer have an obligation not to vouch for his client's false statement by not putting through the prospectus?

MR. FREEDMAN: Good illustration, because it is only through the presumptions imposed by the Commission that the lawyer's silence is so construed. And that is part of the evil in the system that I was discussing before.

You take as a given that silence is construed as vouching. And then you say, once having vouched, shouldn't the lawyer correct the record. And my answer to you is it shouldn't be taken as vouching.

The lawyer should be able to say to the client, "If you do not include that sentence that we are discussing, the Commission would be likely to find it improper, but my research indicates that there is a 50-50 chance that the courts will find that it is not improper." The client then should make the business decision as to whether to go forward, and the lawyer would commit a serious violation of professional responsibility by revealing anything to anybody about it.

Again, I am, for better or worse, the traditionalist and the conservative on this issue. A.A. Sommer and at least three other authorities in the field have called the Commission's view to the contrary "revolutionary."¹¹

MR. SPORKIN: In your hypothetical, Monroe, what do you do now when you catch the client and you find out that the facts were other than

¹¹ Sommer, *supra* note 3 at 4, col. 6.

as pointed out and the information was required to be disclosed. The SEC bring charges against the client, and the client defends on the basis he relied on the advice of counsel.

How do you deal with that problem? The courts seem to be saying more and more that reliance on counsel is a good faith defense. Do you let them off the hook?

MR. FREEDMAN: I'm not aware that it has been established that following advice of counsel is an adequate defense. But certainly if the lawyer were to be called to testify the lawyer would have to testify truthfully unless a privilege were asserted, and the privilege, of course, is the client's.

There's another provision in the Code that I drafted, and it is unique to this Code. That is, that if the lawyer finds that he or she has been put in the position of unwittingly presenting something that is false, because of misrepresentations to the lawyer by the client, the lawyer is permitted to withdraw in, say, an SEC proceeding, as long as that does not involve a direct violation of confidentiality.

QUESTION: I would like to return to the issue of publicity because I think it is so fundamental to the whole enforcement program. You say that on the one hand the public has a right to know, and what you're doing is warning the public that my client, for example, is a bad guy and you ought not to deal with him. My client on the other hand says, "I don't want my reputation ruined by the publicity that will come out when the Commission files the enforcement action."

Now because publicity is so important, I've been very troubled to see on more than one occasion newspaper articles which relate to a pending investigation and which will cite testimony and documents which have been produced in the course of the investigation.

Could you tell what the Commission's policy is with respect to staff attorneys talking to newspaper reporters about any investigations?

MR. SPORKIN: Well, I think you're jumping to a lot of conclusions there.

There is no prohibition against talking to a reporter. A reporter calls, you respond to him. The rule is you can only tell him what's public. If it's not public you can't discuss it with him. You can of course discuss general information and legal concepts with him.

Press reports indicating that somehow somebody has access to a document that was produced in an investigation assume that it had to come from the government.

I want to tell you that we are very concerned about this. I would consider it an extreme breach of faith if any of my people ever provided a reporter with confidential information.

Time and time again we have found in our own investigations that some of that information appearing in the press did not in fact come from a Commission source. It can come from a variety of places. For example, there have been instances in which a witness to a case gets a copy of his

or her testimony and provides that copy to a reporter. There is no rule against that.

Witnesses will talk to the press. There is no prohibition on witnesses talking to the press. And that's where a lot of that information comes from. Sometimes it also comes from Freedom of Information Act requests. Very seldom does the information actually come from the Commission itself; where the Commission has in effect violated that person's right. It is wrong to do it.

QUESTION: I think Mr. Sporkin proved one of Mr. Freedman's points when he demonstrated that he doesn't know about a leading constitutional case. We must also assume that the subordinates in his office do not know leading constitutional cases. They are not trained about the Constitution. Most of the people I have dealt with in such agencies haven't read the Administrative Procedure Act.

I think he also has proved another point that has been made by Justice Jackson: qualities that go to make a good prosecutor are very much the same as those that mark a gentleman. And if a man does not have them, you cannot inculcate them in him. I'm just wondering about Mr. Sporkin's not knowing about the *Alford* case, which all criminal lawyers know about, and his comparing the SEC to a criminal court.

I want to ask if the SEC in its proceedings and in getting consent decrees is operated like a criminal court, why has it been so slow as to be criticized directly by the U.S. Court of Appeals for the D.C. Circuit for not accepting the standard of clear and convincing evidence? Mind you, not the standard of proof beyond a reasonable doubt in criminal cases.

In broker-dealer proceedings and 2(e) proceedings, is the SEC a criminal court? And if so, why don't people before the SEC have all the rights of people involved in criminal proceedings? Furthermore, why are we extending to lawyers who are practicing corporate law in Burling, New Hampshire, Salem, Oregon and all over the country the processes of the SEC with respect to the discipline of attorneys which, under the Administrative Procedure Act, extend only to persons appearing in a representative capacity before the agency?¹²

MR. SPORKIN: I have not read the *Alford* case. But I will read the *Alford* case and see what it says. I like to read the cases myself before I determine exactly what they say.

But, just as I might not have read the *Alford* case, it's obvious that you haven't read the *Steadman* case.¹³

And if you had read the *Steadman* case, you would know that there is another circuit court has held that the preponderance of the evidence test is the appropriate test.

¹² See 5 U.S.C. § 556(d) (1976).

¹³ *Steadman v. Sec. and Exch. Comm'n*, 603 F.2d 1126 (5th Cir. 1979), *aff'd*, 101 S. Ct. 999 (1981).

And if you had kept up with your reading as you assume that every lawyer should, you would know that that issue is presently before the Supreme Court because we, along with the defendants in the case, have petitioned the Court to make a final determination so that we, once and for all, know what is the proper test.¹⁴ And it's going to be the Supreme Court that will make that determination.

QUESTION: If you're going to conduct yourself like a criminal court, you should be applying the proof beyond a reasonable doubt standard, Mr. Sporkin, that's the point. You're trying to have it both ways. And what's involved here is essentially a form of facism, of a bunch of people who have never worked for anyone but the government who think that they are the protectors of the public interest and who therefore have the right to smear people and to conduct their business in any way that they see fit to drive wedges between private parties and their clients and to destroy the legal profession. And that, I submit, is what the SEC and other agencies are trying to do with these proceedings against lawyers.

MR. SPORKIN: I respectfully disagree with you. You can obviously get on any kind of a soapbox you want, but what you're saying is just nonsense, absolute nonsense.

The Supreme Court is going to make that determination as to what the standard is going to be. Not you. And if it's clear and convincing, then that will be the standard. If it is preponderance of the evidence, then it will be preponderance of the evidence.

We're not running a criminal court. I never suggested that we were running a criminal court. I used as examples situations which I know from my everyday life. I've read and I've seen what is happening. And that's all I can tell you.

QUESTION: I have a question for Mr. Freedman. Since the *Alford* case has been tossed around here, it was my understanding that *Alford* did not hold that the defendant has a constitutional right to have a plea bargain in which he is able, after the pleading, to claim his innocence. I believe that was litigated several years ago.

When the Watergate Special Prosecutors Office took a plea from Armand Hammer under an agreement that he would not thereafter claim his innocence, and he thereafter claimed his innocence, the special prosecutor tried to have the verdict set aside. The trial court judge turned it down. And the D.C. Circuit on appeal remanded that case to the District Court with instructions to have Dr. Hammer withdraw his claim of innocence.

I believe it was the formal policy of the Watergate Special Prosecutor's Office throughout his tenure that they would not take plea

¹⁴ In its subsequent decision in the *Steadman* case, the Supreme Court affirmed the appropriateness of the preponderance of the evidence standard in Commission proceedings. *Id.* at 1009.

bargains in the context of *Alford* pleas. I know the matter was litigated once. I'm not sure it was litigated at any other time.

MR. FREEDMAN: That certainly can be the policy of a particular office. It is my view, first—and this is shared by many lawyers who specialize in the securities area—that the Commission has bootstrapped itself into punishments. Imposing a number of penalties that it does not have the statutory authority to impose, and that is done in part through consent decrees.

It is further my view—and the fact that there is a court decision, an intermediate court decision the other way does not give me any pause whatsoever—that it is improper for the government to impose as a condition of accepting a plea the forfeiture of any right, especially a constitutional right, that is not necessarily implicit in foregoing the right to trial by jury.

For example, it has been held by the same United States Court of Appeals for the D.C. Circuit, and elsewhere, that it is professionally improper for a prosecutor to condition acceptance of a *nolle prosequi* or of a dismissal upon a criminal defendant's giving up the right to sue police officers for false arrest or other abusive conduct.¹⁵

It seems to me that the first amendment right to speak is at least as important as the right to file private litigation against a police officer.

The point is that there are limits to the extent to which the Government can properly use its enormous coercive powers. When the state comes after you and says, "If you plead guilty or no contest in order to avoid a potentially harsh penalty, you must not only give up your right to trial by jury, due process, the right to counsel, and other rights that are necessarily implicated, but you must also give up your right to sue a police officer or your right to free speech," that is clearly wrong.

I had a case, for example, in which I was asked by the former Chief Judge of that same Court of Appeals to represent a man who had pled guilty and who was insisting upon his innocence after having served a year in jail.

I got that plea vacated and the Government subsequently decided not to re prosecute him. Under the Commission's rule, that man would have been forbidden to protest his innocence.

* * * *

You know, I have been whip-sawed like this before. If you make a general criticism, then it is characterized as a generalization out of thin air, without supporting specifics. And if you give a specific, it's a war story or it's an anecdote, and doesn't express general or systemic concerns.

MR. SPORKIN: That's not what we're saying. What we're saying is that you are taking one side. You as a lawyer know that you don't

¹⁵ See *Dixon v. District of Columbia*, 394 F.2d 966, 969 (D.C. Cir. 1968).

make a judgment when you hear one side of the case. That's all I'm saying.

I'm not suggesting to you that somebody didn't say what they said to you; but you can't accept that as being true. And that's the worst of the McCarthy tactics.

MR. FREEDMAN: That betrays a certain lack of understanding of what McCarthyism is.

What I have here, I'll show to you, I'll show to anybody in the audience, I'll give to the gentleman who is reporting. It's a letter on SEC letterhead to an individual, signed by Jack H. Bookey, Regional Administrator of the SEC.

It says:

"The Wall Street Journal of January 14, 1980, has quoted you as saying that your firm 'agreed to limited sanctions. Obviously we don't consider we've done anything that's out of order, but we compromised the issue by entering into the agreement we did.' " Also, "The Seattle-Times quoted you as saying that you agreed with the censure because it could cost thousands of dollars to oppose it.

* * *

"It is the Commission's policy not to permit respondents in an administrative proceeding to consent to an order imposing a sanction while denying the allegations. It is important to avoid creating an impression that a decree is being entered or a sanction imposed when the conduct alleged did not in fact occur.

"Accordingly, if you make any more public statements along these lines, *in or out of court*, we will bring them to the attention of the Commission for consideration of appropriate action."

That is chilling first amendment rights. That's not even a close question. Mr. Sporkin says that I decide what's constitutional. I have practiced and taught in the constitutional law area for a quarter of a century. I'm entitled to make those judgments. The difference between us is that when I make a judgment about a constitutional right, nobody gets his name smeared in the press; nobody has to spend tens or hundred of thousands of dollars defending him or herself, when in too many cases it shouldn't have been necessary in the first place.

If you want to see this letter, if somebody believes I'm just waving it in a McCarthy-like fashion, just come up and take it please.

MR. SPORKIN: But do you think that it would be improper for the agency to have a policy that says we will not accept consent decrees from people who want to deny that they've engaged in that conduct? Would that be inappropriate for the SEC to do?

MR. FREEDMAN: Yes it would.

If you say we are going to reach out beyond the confines of this con-

sent agreement, and we are going to tell you what you can say to the Wall Street Journal or the Seattle-Times about this case because we don't want people to get a bad impression of our enforcement policies, that is what the First Amendment to the Constitution is about.

MR. SPORKIN: I've got to go back.

You're saying that there's a constitutional right for anybody who is charged with a violation to enter into a consent decree. Is that what you're saying?

MR. FREEDMAN: Of course not, Stanley, you know that. What I'm saying is that there are limits to the proper scope of a consent decree and you shouldn't be bootstrapping yourself into powers that were not given you by statute, and indeed powers that could not be given you by statute.

If the Congress were to write a law saying the SEC can let you off the hook if you give up your free speech right to talk to the Wall Street Journal about your case, that law would be unconstitutional.

MR. SPORKIN: By the way, you have not escalated this to say you can't talk to them about the case and nobody said that. You're mischaracterizing it. And I hope you haven't mischaracterized the *Alford* case the way you've done that. You can talk to a reporter any way he wants, and any time he wants concerning the case.

You know, you're there on the one side criticizing the agency for doing too much. We got, on the other hand, Business Week and other publications and Barrons that are criticizing the agency because we engage and enter into consent decrees, and indicating that we ought to be litigating more of these things. We ought to be determining whether somebody has done these things.

MR. FREEDMAN: I agree. I think plea bargaining and consent decrees is an utterly offensive process. I know the Court has approved it. I will do it for a client. I'm not saying a lawyer acts improperly when it's in a client's interest to enter one of these agreements.

I even—heaven help my civil libertarian soul—I even advised a client who consented that if we issued a particular press release about the case, that there was a chance that the Commission would come after him again. And on that advice my client indeed had his first amendment rights chilled. He said, "Let's not issue it then, if that's the case." I've seen it happen.

But the fact that one will engage in these practices if they are made part of the system, is not an argument that they should be part of the system.

You are arguing again from that which is, to that which ought to be. Because it is, that doesn't mean it ought to be.

MR. SPORKIN: I'm confused. Are you now suggesting that someone under the Freedman "ought to be" plan can't settle his case with the SEC or any other government agency?

MR. FREEDMAN: I'm saying that there are or there should be

limits on the sanctions that the Commission can impose as part of such a consent.

MR. SPORKIN: There is, by consent. You can't impose anything more than what the other person has agreed to have imposed. It's not something the Commission is ordering: This is a consensual arrangement. Every day in this land there are private parties that are settling cases.

MR. FREEDMAN: Justice Holmes pointed out that the essence of duress is that somebody is making a choice in accordance with his or her interest, but it is still duress. Yes, people consent. People consent because the screws are too tight.

MR. SPORKIN: You know, you talk about forty, fifty percent. What do you think is the percentage of consent decrees in which people have actually done what this big, bad agency says they did? What's your percentage on that? Would you hazard a guess? Would you say it's ninety-nine percent?

MR. FREEDMAN: The theory underlying the Bill of Rights is that it is better for nine of those bad people to go free than one innocent person be coerced into consenting or otherwise suffering penalties unfairly.

MR. SPORKIN: So in other words we've got to do away with our mandate to protect the public because we are ninety-nine percent right. If we're one percent wrong you can do away with the agency. That's anarchy.

QUESTION: I'm addressing this in the context of a concerned investor, that is, somebody who wants to know who I'm doing business with. This is in the context of researching a question on ancillary remedies which might be available in an injunctive proceeding, and I find in the *Harvard Law Review* this illustration. It was in the context of the SEC enforcement action where the defendant was successful in convincing the judge that he should not appoint a receiver but that he might specify certain things that the defendant would do and thereby forego the need and the embarrassment and the expense of having to have a receiver appointed.

The footnote then picks that up and says that the restrictions included prohibitions against the sale of notes and stock without proof of exemption from registration requirements, prohibitions on the investment or reinvestment of funds without extensive disclosures, et cetera.

The note then goes on to say that in addition to these restrictions, the court ordered the defendant to send to shareholders copies of the court's opinion and order in order that the investors may be fully and fairly informed as to the status of the case, possible legal remedies they may have and its possible effect on their investment.

Before mailing the material the defendant sent a newsletter to the shareholders which began—and this is all in big, bold quotes: "Good news, we won. We beat the SEC."

The court concluded that this newsletter was seriously deceptive and was intended to mislead investors as to the corresponding court order and lull them into a false sense of security. It discouraged them from reading the subsequently distributed and much lengthier opinion and order and as a result, a receiver was appointed in subsequent proceedings.

And I ask you, do you as a civil libertarian, do you feel that the court was unreasonably impinging upon this individual's first amendment rights? Thinking in terms of me as an investor, I would like to know so that when I go to deal with people who are holding themselves out as being reputable, I can be sure that they are in fact reputable.

MR. FREEDMAN: I have concerns with that case, but not at all the same as I have when it is done by the agency and not by a court after a finding of culpability, of liability. What you are suggesting is a case in which the respondent appears to have been attempting to flout the order of the court. Assuming that the order of the court was a proper one, based on the evidence and within the power of the court to issue, you have a very strong case for preventing the respondent from flouting that order.

But I have difficulties with the order itself, because it requires a private party to speak or not to speak, and I have serious questions as to whether the court has that power. The court might authorize the SEC, for example, to publicize that finding of liability, but I have a good deal of difficulty about ordering a private party to say or not to say something.

For example, in a case about three years ago, the Supreme Court (not a notoriously civil libertarian court) held unanimously that even where a newspaper had committed a libel against an individual, the State of Florida could not require that newspaper to publish a correction, because part of freedom of speech is not simply the right to speak, but the right not to speak.¹⁶ When a court says to somebody, "You shall speak and tell them thus-and-such," I think that exceeds the constitutional powers of the court. Therefore, the second part would fall with it.

If the court has the initial power then you have a stronger case for the second one. But whether the Commission has this power statutorily, or could constitutionally be given it in the context of consent agreements, I have a great deal of doubt.

QUESTION: Well, isn't the Commission taking the 10b-5 approach? If you deliberately omit a material fact in terms of trying to convince somebody to buy your stock, have not you in fact done what Congress legislated? In effect what you're saying is that your first amendment rights are out the window on that one, Charlie. If you're going to tell people when you want to sell something, you have to tell the whole truth and nothing but the truth.

¹⁶ See *Miami Herald Publishing Co. v. Tornello*, 418 U.S. 241, 256 (1974).

MR. FREEDMAN: If you are obtaining something of value from somebody else through deceitful means that, in common law terms, has been subject to state punishment. When the Commission admits that the reason it is not permitting you to speak is that it doesn't want people to get a bad impression of our enforcement policies, you're not talking about protecting investors, you're talking about protecting a government agency in the way it carries on its obligations to the people. That's a very different matter.

QUESTION: But is that really the matter or is it because they don't want the investor going back to this person who has consented to an injunction and whose books and records admit that he is not financially capable of carrying on a business? Isn't it more in the interest of the public to let the public know that so that they might want to assess whether or not to do business with this individual rather than trying to protect their reputation and having accepted an unwitting consent decree?

MR. FREEDMAN: If it can be shown that somebody is being deprived of something of value by deceitful statements, then there would be a different case. When the government official himself says that a purpose is that they do not want the respondent to create a false impression of our enforcement program, I think that lets the cat out of the bag.

It's a little bit like Nixon saying it is all in the interest of national security that we're not telling you what you want to know. The real reason is not national security, it's protecting the public official from criticism, and here Chairman Williams is saying it right up front.

QUESTION: My impression from that statement as you read it would be that he's concerned about the public thinking that it is now okay to go back and do business with this guy because he has set the record straight as far as the SEC is concerned.

MR. FREEDMAN: You read a long list of things that he is now going to do that apparently are corrections of all the bad things he was doing, and so I suppose people can now invest with him in safety. Otherwise, what the courts should have done was not impose these conditions, but suspend him.

QUESTION: What sanctions have been sought and have been applied where someone does violate a consent by, in the Commission's view, violating consent by making a public statement afterwards?

MR. SPORKIN: I don't think very much, if anything, as I recall. I think there is one case where somebody misrepresented what the court decision was and we went into court to have it corrected and we prevailed.

Consent negotiations are normally very civilized. The way this thing comes out now is that you sit down with people. It used to be that prospective defendants would want to deny charges in the consent papers. The Commission published a statement some years back that states if

you want to consent you cannot deny the allegations. You must indicate that you are neither admitting nor denying them.

You then tell people who want to consent, "Look, are you prepared to consent on that basis or not?" If they are not prepared to do it on that basis, they can't get a consent decree. You litigate.

You also tell these people that the decree doesn't admit or deny anything today but it doesn't mean that tomorrow you can come out and deny this. If in fact the person does it, you speak to the person and ask him if he's serious about it, does he really want to deny the charges. If he does, then we would suggest that we both go to the court and dissolve the consent decree and litigate the matters. Usually the word comes back to us that it was somebody down the line who didn't know what he was doing that put out the release.

Lawyers usually are very knowledgeable in this area and they usually make sure that the client understands that the SEC is for real. They don't want to take advantage of anybody. The consent process is misunderstood. What the SEC is trying to do in a spirit of decency, honesty and fairness is now being turned around as being something dirty or something wrong. This is very bothersome to me.

When you really look at it, Monroe, this wasn't Stan Sporkin who was concerned about this. This was the Chairman of the Commission, a person from the private sector who looked at the system and said, "You know, it is unfair, Stan, for somebody to come in here and consent without admitting or denying, and then tomorrow to go out and deny everything. It just is unfair." And the Chairman is right. If someone says he hasn't done what we said he did, let's litigate the case.

So you've got to realize—I'm sorry we spent so much time on this issue because I really don't think it's a problem. But maybe others do think it is a problem.

MR. FREEDMAN: I guess the point of the question was that there is something false and misleading, or at least bordering upon it, when the respondent says we won when, in the questioner's view, the respondent didn't really win.

QUESTION: Maybe in his mind he did win.

MR. FREEDMAN: I agree. That's one of the reasons I have a problem with it. But let me direct a question to those lawyers in the audience who are particularly sensitive to false and misleading statements; you know, not outright lies, but things that will mislead people.

What about the respondent who enters a consent, neither admitting nor denying the allegations of the complaint, and the SEC publicizes that, along with every detail of the complaint.

Isn't it likely that there are some people out there, investors, who might be misled into thinking that the consent reached every one of those allegations in the original complaint? Have there not indeed been prominent and reputable citizens who have been hurt by that kind of practice and hurt very badly by it?

III. CLOSING STATEMENTS

MR. SPORKIN: To answer your question, Monroe, again the person consenting must know and understand exactly and precisely what he's doing. We don't agree not to publicize the case; that would be ridiculous. If we have to, we'll litigate the case. We're not afraid to litigate cases.

As I said at the outset, I think that when you're evaluating an agency, you have to evaluate it on the basis of whether it has conducted its work with respect to the mission that Congress has imposed upon it. It's unfortunate that we start getting into the nuts and bolts and we lose sight of that.

And I want to again remind you that I think we've done a pretty good job. I want to again remind you that the kinds of things that Monroe is saying here are not practices that permeate the whole system and somehow make the system wrong.

Indeed, I think when you have our system scrutinized along with others, that you're going to find that the SEC has one of the most fairly conducted programs in government.

I, like Monroe, am a very deep believer in civil rights. He was right in the beginning when he indicated how deeply I feel about these matters. In numerous instances where we believed that the Commission could be deemed to be unfair to somebody, we have backed away. We haven't taken advantage of people. I don't want to take advantage of anybody. I want everybody to be right up front when we sit down to discuss a case and to understand where we're coming from. What is terribly troubling to me is that Monroe and I have such divergent viewpoints that it's almost like we're trying to incorporate a system from Mars into the system of the United States, and that makes it very difficult for me to accept.

I can't deal with somebody if I'm up front with that person and that person is misleading or lying to me because it's his duty and role to mislead me. I can't run a business that way; nobody can run a business that way.

As I said in answer to one of the questions, I must tell you as an attorney, as a member of the Bar, that as soon as we detach what is common decency, what is honesty, what is fairness, what are, as we all know, good ethics, from reality, as the proposed code that Mr. Freedman is talking about will do, then the system comes to a halt. You can't ask people to do something that doesn't make sense and have it carried out. You can't have lawyers who are suborning perjury. You can't have lawyers who are going to lie and mislead and so conduct themselves.

It may well work in other areas. It cannot work in the securities field, where the whole underpinning of the entire system depends upon candor, depends upon disclosure, depends upon honesty, depends upon being truthful to people.

I really submit to you that I think that the whole system here depends upon openness and candor. That your system, Monroe, really doesn't fit in here. And I think it's unfortunate, but I think that's the way it is.

MR. FREEDMAN: There are two things that I want to say preliminarily in these closing remarks:

Just as, six years ago, I went out and spoke to some prominent and knowledgeable practitioners about the SEC, I revisited some of those people and some others in the past few weeks, as well as reading the Enforcement Training Program Manual.

One of the things that has come up consistently in the comments that I have gotten from lawyers, including the ones that I had been to six years ago, is that enforcement abuses are not what they were six years ago, that there has been improvement. For example, previously, witnesses were being told by members of the staff not to talk to the lawyer on the other side. Not only did that not happen in a case where I had occasion to look into it, but I've spoken to other lawyers, including the lawyers who have complained about it previously, and that practice has stopped.

I think it is to the credit of Mr. Sporkin and to the agency that there has been improvement. There has been retrogression, however, in the stepped-up emphasis on 2(e) proceedings, and the effort to expand them, and I think that those problems are in a way more serious.

Another thing impressed me, because it is a cliché among the private Bar that the only lawyers one cannot trust to keep one's word after having made an agreement are prosecutors. I don't know that I've ever spoken to a lawyer in private practice who did not feel that way, that while another lawyer in private practice will stick to his or her agreement, a prosecutor can't be trusted.

A prominent member of a major firm who has done considerable work before the SEC said to me, "One thing I'll say about Stanley Sporkin, he keeps his word. He's a hard man to pin down, but once you've pinned him down you can trust him." I think that's an important thing. At the same time, I don't feel satisfied that the criticisms that I have made have been adequately met and answered.

I have complained about the efforts to co-opt the private Bar. I have quoted from a number of Commissioners and from SEC opinions to that effect.

And Stanley's response has been, in effect, we can't really succeed in co-opting the members of the private Bar; who in this audience has ever been co-opted by us? But he didn't deny or disavow those quotes, which show that the effort is being made.

Indeed, I think the co-option of the private bar is illustrated by Mr. Sporkin's evasive answer to the hypothetical case I put. If a lawyer gives his or her best professional advice to a client, and the client then

makes its own judgment on the basis of that advice, the lawyer may be in jeopardy for not reporting the client's possible violation to the SEC.

With regard to my statement that I have been through the Manual and that there is an inadequate program or non-existent program of training for lawyers at the investigative stage, I think it's significant that Mr. Sporkin has not denied that. I would expect, though, that there is something that may well be corrected in the future.

With regard to the problems of abusive publicity, Mr. Sporkin has defended that on the grounds that publicity protects the public. What that means, however, in the context of the pretrial or prehearing stage, is that the SEC is protecting the public by warning the public that this is somebody you don't want to deal with. If you're not communicating that, you're not protecting them. That means, necessarily, that you are protecting them by damaging the reputation and the business of somebody who has not yet been found through due process to be someone they have to be protected against. You are smearing, you are destroying, someone's reputation without due process.

The only response Mr. Sporkin has to that is, "We're getting away with it. Do you expect the Supreme Court to slap us down on that?" Perhaps the answer is no, although maybe Stanley and I will have it out someday, and find out.

With regard to the chilling of free speech, I did not hear any response, except, "They consent to it." Justice Holmes has made the point that it is in the nature of duress that you consent to it. Your ship is sinking, lives are going to be lost. The salvor comes along and says, "I'll tow you in, and save your lives, but you've got to give me the ship when you get into port." When the captain says, "Okay, it's a deal," the captain knows what he's doing. The problem is that while he knows what he is doing, he also knows he is doing it under duress. What I'm submitting to you is that there is duress in the system, a major piece of it being the very damaging pretrial, prehearing publicity.