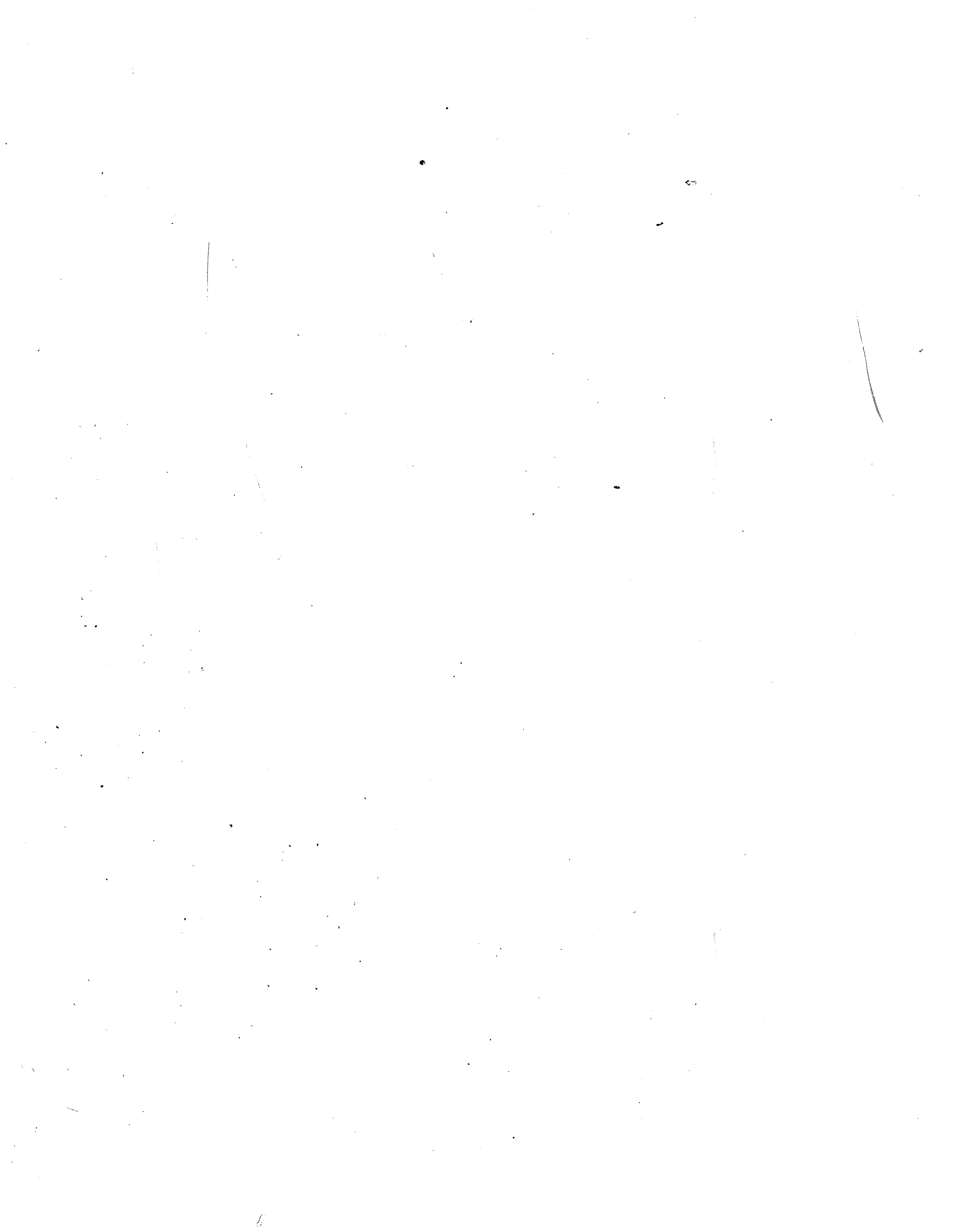

The New York Times

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BUSINESSES SEEK NEW PROTECTION ON LEGAL FRONT

CIVIL AND CRIMINAL CASES

Trying to Sway Pendulum, With Encouragement of Administration

By STEPHEN LABATON

WASHINGTON, Oct. 28 — Frustrated with laws and regulations that have made companies and accounting firms more open to lawsuits from investors and the government, corporate America — with the encouragement of the Bush administration — is preparing to fight back.

Now that corruption cases like Enron and WorldCom are falling out of the news, two influential industry groups with close ties to administration officials are hoping to swing the regulatory pendulum in the opposite direction. The groups are drafting proposals to provide broad new protections to corporations and accounting firms from criminal cases brought by federal and state prosecutors as well as a stronger shield against civil lawsuits from investors.

Although the details are still being worked out, the groups' proposals aim to limit the liability of accounting firms for the work they do on behalf of clients, to force prosecutors to target individual wrongdoers rather than entire companies, and to scale back shareholder lawsuits.

The groups hope to reduce what they see as some burdens imposed by the Sarbanes-Oxley Act, landmark post-Enron legislation adopted in 2002. The law, which placed significant new auditing and governance requirements on companies, gave broad discretion for interpretation to the Securities and Exchange Commission. The groups are also interested in rolling back rules and policies that have been on the books for decades.

To alleviate concerns that the new Congress may not adopt the proposals — regardless of which party holds power in the legislative branch next year — many are being tailored so that they could be adopted through rulemaking by the S.E.C. and enforcement policy changes at the Justice Department.

The proposals will begin to be laid out in public shortly after Election Day, members of the groups said in recent interviews. One of the committees was formed by the United States Chamber of Commerce and until recently was headed by Robert K. Steel.

Mr. Steel was sworn in last Friday as the new Treasury undersecretary for domestic finance, and he is the senior official in the department who will be formulating the Treasury's views on the issues being studied by the two groups.

The second committee was formed by the Harvard Law professor Hal S. Scott, along with R. Glenn Hubbard, a former chairman of the Council of Economic Advisers for President Bush, and John L. Thornton, a former president of Goldman Sachs, where he worked with Treasury Secretary Henry M. Paulson Jr.

That group has colloquially become known around Washington as the Paulson Committee because the relatively new Treasury secretary issued an encouraging statement when it was formed last month. But administration officials said Friday that he was not playing a role in the group's deliberations.

Its members include Donald L. Evans, a former commerce secretary who remains a close friend of President Bush; Samuel A. DiPiazza Jr., chief executive of PricewaterhouseCoopers, the accounting giant; Robert R. Glauber, former chairman and chief executive of the National Association of Securities Dealers, the private group that oversees the securities industry; and the chief executives of DuPont, Office Depot and the CIT Group.

Jennifer Zuccarelli, a spokeswoman at the Treasury Department, said on Friday that no decision had been made about which recommendations would be supported by the administration.

"While the department always wants to hear new ideas from academic and industry thought leaders, especially to encourage the strength of the U.S. capital markets, Treasury is not a member of these committees and is not collaborating on any findings," Ms. Zuccarelli said.

But another official and committee members noted that Mr. Paulson had recently pressed the groups in private discussions to complete their work so it could be rolled out quickly after the November elections.

Moreover, committee members say that they expect many of their recommendations will be used as part of an overall administration effort to limit what they see as overzealous state prosecutions by such figures as the New York State attorney general Elliot Spitzer and abusive class action lawsuits by investors. The groups will also attempt to lower what they see as the excessive costs associated with the Sarbanes-Oxley Act.

Their critics, however, see the effort as part of a plan to cater to the most well-heeled constituents of the administration and insulate politically connected companies from prosecution at the expense of investors.

One consideration in drafting the proposals has been the chain of events at Arthur Andersen, the accounting firm that was convicted in 2002 of obstruction of justice for shredding Enron-related documents; the conviction was overturned in 2005 by the Supreme Court. The proposals being drafted would aim to limit the liability of auditing firms and include a policy shift to make it harder for prosecutors to bring cases against individuals and companies.

Even though Arthur Andersen played a prominent role in various corporate scandals, some business and legal experts have criticized the decision by the Bush administration to bring a criminal case that had the effect of shutting the firm down.

The proposed policies would emphasize the prosecution of culpable individuals rather than corporations and auditing firms. That shift could prove difficult for prosecutors because it is often harder to find sufficient evidence to show that specific people at a company were the ones who knowingly violated a law.

One proposal would recommend that the Justice Department sharply curtail its policy of forcing companies under investigation to withhold paying the legal fees of executives suspected of violating the law. Another one would require some investor lawsuits to be handled by arbitration panels, which are traditionally friendlier to defendants.

In an interview last week with Bloomberg News, Mr. Paulson repeated his criticism of the Sarbanes-Oxley law. While it had done some good, he said, it had contributed to "an atmosphere that has made it more burdensome for companies to operate."

Mr. Paulson also repeated a line from his first speech, given at Columbia Business School last August, where he said, "Often the pendulum swings too far and we need to go through a period of readjustment."

Some experts see Mr. Paulson's complaint as a step backward.

"This is an escalation of the culture war against regulation," said James D. Cox, a securities and corporate law professor at Duke Law School. He said many of the proposals, if adopted, "would be a dark day for investors."

Professor Cox, who has studied 600 class action lawsuits over the last decade, said it was difficult to find "abusive or malicious" cases, particularly in light of new laws and court decisions that had made it more difficult to file such suits.

The number of securities class action lawsuits has dropped substantially in each of the last two years, he noted, arguing that the impact of the proposals from the business groups would be that "very few people would be prosecuted."

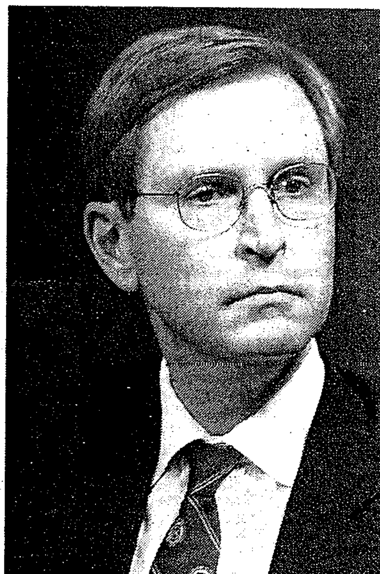
People involved in the committees said that the timing of the proposals was being dictated by the political calendar: closely following Election Day and as far away as possible from the 2008 elections.

Mr. Hubbard, who is now dean of Columbia Business School, said the committee he helps lead would focus on the lack of proper economic foundation for a number of regulations. Most changes will be proposed through regulation, he said, because "the current political environment is simply not ripe for legislation."

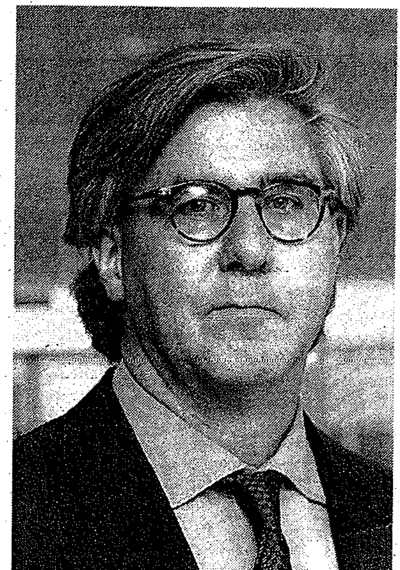
But the politics of changing the rules do not break cleanly along party lines. While some prominent Democrats would surely attack the pro-business efforts, there are others who in the past have been sympathetic.

People involved in the committees' work said that their objective was to improve the attractiveness of American capital-raising markets by scaling back rules whose costs outweigh their benefits.

"We think the legal liability issues are the most serious ones," said Professor Scott, the director of the committee singled out by Mr. Paulson. "Companies don't want to use our markets because of what they see as the substantial, and in their view excessive, liability."



Stephen Hilger/Bloomberg News



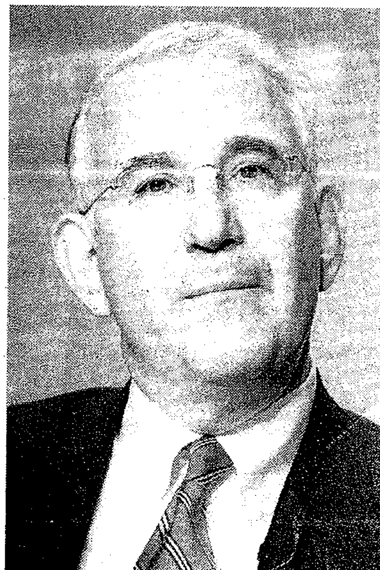
Hiroko Masuike for The New York Times

Leading the groups hoping to scale back regulation are R. Glenn Hubbard, dean of Columbia Business School, left, and John L. Thornton, a former president of Goldman Sachs.

Adam Berry/Bloomberg News

David McIntyre/Bloomberg News

Other leaders include Robert Glauber, a former NASD chairman, left, Donald Evans, a former commerce secretary, right, and Samuel DiPiazza, chief executive of PricewaterhouseCoopers, below.



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Committee officials disputed the notion that they were simply catering to powerful business interests seeking to benefit from loosening regulations that could wind up hurting investors.

"It's unfortunate to the extent that this has been politicized," said Robert E. Litan, a former Justice Department official and senior fellow at the Brookings Institution who is overseeing the committee's legal liability subgroup. "The objectives are clearly not to gut such reforms as Sarbanes-Oxley. I'm for cost-effective regulation."

The main Sarbanes-Oxley provision that both committees are focusing on is a part that is commonly called Section 404, which requires audits of companies' internal financial controls. Some business experts praise this section as having made companies more transparent and better managed, but many smaller companies call the section too costly and unnecessary.

Members of the two committees said that they had reached a consensus that Section 404, along with greater threat of investor lawsuits and government prosecutions, had discouraged foreign companies from issuing new stock on exchanges in the United States in recent months.

The committee members said that an increase in stock offerings abroad was evidence that the American liability system and tougher auditing standards were taking a toll on the competitiveness of American markets. But others see different reasons for the trend and few links to liability and accounting rules.

Bill Daley, a former commerce secretary in the Clinton administration who is the co-chairman of the Chamber of Commerce group, expects proposed changes to liability standards for accounting firms and corporations to draw the most flak. But he said that the changes affecting accounting firms are of paramount importance to prevent the further decline in competition. Only four major firms were left after Andersen's collapse.

Another contentious issue concerns a proposal to eliminate the use of a broadly written and long-established anti-fraud rule, known as Rule 10b-5, that allows shareholders to sue companies for fraud. The change could be accomplished by a vote of the S.E.C.

John C. Coffee, a professor of securities law at Columbia Law School

In a post-election effort, some business leaders want a lighter regulatory burden.

and an adviser to the Paulson Committee, said that he had recommended that the S.E.C. adopt the exception to Rule 10b-5 so that only the commission could bring such lawsuits against corporations.

But other securities law experts warned that such a move would extinguish a fundamental check on corporate malfeasance.

"It would be a shocking turning back to say only the commission can bring fraud cases," said Harvey J. Goldschmid, a former S.E.C. commissioner and law professor at Columbia University. "Private enforcement is a necessary supplement to the work that the S.E.C. does. It is also a safety valve against the potential capture of the agency by industry."