

TRUST THE LEADERS

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Bringing New Hope for the
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WINTER 2002 ISSUE 2

editor in chief

Terry Ferraro Schwartz

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Smith, Gambrell & Russell's marketing team

**Connie Frost, Andy Carlyle,
Kathy Hay**

contributing writers

**Scott Cahalan, Linda Dunlavy,
Jacob Frenkel, Stephen Fusco, Ira Genberg,
Kristen Lewis Denzinger, Tim Johnson, Joyce Klemmer,
Brett Lockwood, Tamara Mosashvili-Shevardnadze,
Dana Richens, Marlon Starr, Den Webb,
Ron Wells, Kathy Zickert**

design agency

**CreativeBeast Marketing Communications, Inc.
Atlanta, GA**

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SMITH, GAMBRELL & RUSSELL, LLP
ATTORNEYS AT LAW

Promenade II, Suite 3100
1230 Peachtree Street, N.E.
Atlanta, GA 30309-3592
e-mail: editor@sgrlaw.com

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A Rude Awakening FOR CORPORATE AMERICA



The summer of 2002 was quite jarring for senior management of public companies, domestic and foreign, which are subject to U.S. securities laws – and for the attorneys practicing securities law, myself included. An order from the Securities and Exchange Commission in June, followed by the passage of the Sarbanes-Oxley Act of 2002 on July 30 and more rule-making by the SEC in August, have dramatically focused attention on individual officer accountability for the disclosures made by public companies in their reports filed with the SEC. Special detailed officer certifications are now required to accompany each quarterly and annual report filed, among other new rules and regulations. Although we securities lawyers can argue that the chief executive officers and chief financial officers of public companies have had responsibility for their companies’ disclosures (and attendant risk of personal liability) since the passage of the Securities Act of 1933 and the Securities Exchange Act of 1934, Sarbanes-Oxley appears to have effected a “sea change” in the perception of personal risk by officers and directors. Congress and the White House obviously intended to achieve that result in the wake of the corporate scandals of 2001-2002. Sarbanes-Oxley also has significant executive compensation implications. Thus we chose for our feature article Sarbanes-Oxley and some of its ramifications.

This issue also reviews the benefits of the use of “special needs trusts,” which are critically important to the funding and management of life-care plans for disabled persons who require long-term care and financial support. Most of us either have, or know someone who has, a loved one or friend who faces these special challenges. A variety of other topics are featured, including the introduction of a new form construction contract for owners and developers, a review of the zoning and land-use process for large-scale real estate developments, and a look at European data privacy laws.

To date, our readers’ comments on Issue 1 of our magazine have been overwhelmingly positive (I hope it’s not just beginner’s luck!) and are greatly appreciated. Your input and feedback are welcome and valuable to us.

It is hard to believe that another year is coming to a close – jam-packed with school back in session, sports events to attend, and the holidays upon us – and as our next issue will not be published until early next year, we at SGR would like to take this opportunity to wish you a safe, happy and prosperous end of 2002 and beginning of 2003.

Terry Ferraro Schwartz
Editor in Chief
editor@sgrlaw.com

Special Needs Trusts

Planning for the disabled population is an emerging legal specialty bringing new hope to the physically and mentally challenged.

Many of us have a relative, friend or colleague who is challenged on a daily basis by some type of incapacitating physical, mental or developmental disability. In days past, the families of disabled persons often kept their personal circumstances a secret; the disability of their loved one was a taboo subject that was not to be discussed openly. To make matters worse, there were very few competent professional advisors available to help plan for the “special needs” of disabled persons. Left on their own, many disheartened families had limited options to ensure appropriate care for disabled relatives after their primary caregivers died or grew too old and infirm to provide the necessary care.

New Hope for the Disabled

Happily, much has changed in the emerging area of planning for the disabled. Law schools now routinely offer courses which address the numerous specialized needs of people who are disabled. As a consequence, the number of lawyers focusing on elder law, disability planning and government benefits planning has increased dramatically. These specialized lawyers are able to render legal advice that more fully meets the needs of the disabled community. Joining forces with these lawyers is an array of allied professionals, such as life-care planners, rehabilitation specialists, disability-specific support groups, and legislative advocates for the disabled. Together, they provide ready access to valuable resources for persons of all ages who are challenged by incapacitating disabilities. (As an example, see the sidebar regarding the innovative “Virtual Resource Center” being developed by the Georgia Brain Injury Association.)



Public-Private Funding of Special Needs

One of the biggest concerns voiced by families of persons with disabilities is how best to fund their long-term personal and financial needs in a manner that will secure for them a full – and fulfilling – lifestyle geared to their specific abilities and preferences. Increasingly, lawyers are recommending a flexible and effective option to provide for the immediate and future benefit of disabled persons: the “Special Needs Trust” (SNT). This planning vehicle can be established and customized to address the unique circumstances of each family faced with the daunting task of securing the future of a disabled loved one. Careful drafting of the SNT can allow the disabled beneficiary to become and remain eligible for need-based government benefits, such as Medicaid and Supplemental Security Income, which often serve as a significant source of funding for the disabled beneficiary’s special needs.

FEDERAL AND STATE LAWS PERMIT, AND EVEN ENCOURAGE, SNT PLANNING WHICH MAXIMIZES THE USE OF ALL AVAILABLE RESOURCES. IN ORDER TO PROVIDE FULLY FOR THE NEEDS OF THE DISABLED.

Contrary to popular belief, such government benefits are not just for the poor. Federal and state laws permit, and even encourage, SNT planning which maximizes the use of all available resources, both private and governmental, in order to provide fully for the needs of the disabled. For persons of limited means, government programs may constitute the primary source of funding for their current and future needs. Surprisingly, government assistance is often also available to families with more significant resources to help meet certain basic needs of their disabled relatives. These families can then utilize their personal resources to provide for non-basic needs and quality of life enhancements. Thus, the disabled person first taps into any government benefits to which he or she is entitled, and then the family's private assets serve as a secondary source of support to supplement – not supplant – such government benefits. Families from all economic backgrounds hail this public-private partnership as an effective means of funding the special needs of disabled persons. The cornerstone of this partnership is the SNT.



To determine which type of SNT is most appropriate for a disabled Beneficiary, the primary consideration is whether the assets and resources belonging to, or otherwise available to, the Beneficiary are likely to cover fully the cost of supporting and caring for the Beneficiary during his or her lifetime. If such assets and resources are likely to be sufficient, then a General Support SNT may be appropriate. However, if the Beneficiary's assets and resources are inadequate to fund fully all of the special needs of the Beneficiary (as is more often the case), and need-based government programs

could constitute a critical part of funding the Beneficiary's needs, then a Supplemental Care SNT may be in order. Most families who undertake SNT planning desire to maximize all available resources, including government programs. For that reason, the Supplemental Care SNT is by far the more frequent choice.

Flexible and Comprehensive Care

“Special needs” is a broad term encompassing not only medical and health-care services and products which may benefit a disabled Beneficiary,

but also a wide range of related services and “quality of life” options which may be tailored to the particular circumstances of the Beneficiary. For example, once a Beneficiary's medical needs are adequately provided for, the SNT may help fund the cost of additional service providers, such as domestic and personal assistants to aid the Beneficiary with the “activities of daily living,” or attendant and respite care to give the Beneficiary's primary caregiver a much needed break. The SNT can purchase a customized, accessible van or other vehicle appropriate for the Beneficiary's circumstances, and pay the cost of the maintenance, insurance and periodic replacement of the vehicle. Similarly, SNT assets can be used to pay for beneficial living arrangements, including additions or renovations to the Beneficiary's residence to render it accessible, the cost of a communal or assisted-living arrangement, or a “luxury” skilled nursing facility.

Which Special Needs Trust Is Best?

Typically, the SNT is set up as a fund which is privately and professionally managed and administered by a corporate Trustee for the sole benefit of a person with disabilities or other impairments (the Beneficiary). There are two basic types of SNTs: a General Support SNT, and a Supplemental Care SNT. The vast majority of SNTs are Supplemental Care SNTs, which are designed to serve as a secondary source of benefits for the Beneficiary after all available government benefits have been exhausted. The assets of a properly drafted Supplemental Care SNT are not considered “available resources” for purposes of qualifying the Beneficiary for need-based benefits. By contrast, any property in a General Support SNT – which is designed to serve as the primary or sole source of benefits for the Beneficiary – would be considered an available resource of the Beneficiary, which can preclude eligibility for need-based benefits.

Other common SNT disbursements include funds for:

- ✦ appropriate recreational and vocational activities;
- ✦ hobbies and vacations;
- ✦ educational and training opportunities;
- ✦ augmentative communication equipment;
- ✦ professional services for the Beneficiary, including attorneys, accountants and claims processors; and
- ✦ procurement and maintenance of a pet or service animal for the Beneficiary.

Permissible disbursements from a SNT are limited only by the creativity of the drafting attorney and the overriding requirement that the Beneficiary derive the primary benefit therefrom.

Establishing and Funding a Special Needs Trust

The SNT may be established under a Last Will and Testament, or inter vivos (i.e., during life). It may be funded by a third party (such as a parent or other relative) or funded with the assets of the Beneficiary. If the SNT is “self-settled” – funded with the Beneficiary’s own assets – federal law requires that the SNT must provide for the reimbursement of Medicaid (or other government medical providers) at the death of the Beneficiary from the property then remaining in the SNT (if any), up to the full amount of medical benefits previously paid on behalf of the Beneficiary. Only after this “payback” requirement is fulfilled may other persons – such as the descendants or siblings of the deceased Beneficiary – share in any remaining Trust property.

There are two additional requirements under federal law for a qualifying, self-settled Supplemental Care SNT:

- ✦ The Beneficiary must be “disabled” within the meaning of the Social Security Act, i.e., unable to engage in any substantial gainful activity as a result of his or her disability; and
- ✦ the Beneficiary must be under age 65 when the SNT is established and funded (or subsequently augmented) with the assets of the Beneficiary.

For persons who are over age 65 when a self-settled Supplemental Care SNT is desired, federal law provides only one option: a “pooled” SNT in which numerous disabled persons of any age may participate. In Georgia, such a pooled SNT is operated under the auspices of The



Canine Assistants

Canine Assistants, based in Alpharetta, Georgia, is a nonprofit organization which trains and provides service dogs for children and adults with physical disabilities or other special needs. Some of the tasks performed by service dogs include turning lights on and off, opening and closing doors, pulling wheelchairs, retrieving dropped objects, summoning help and providing secure companionship. By state and federal law, service dogs are permitted to accompany their disabled recipients in all public venues, with only two exceptions: a medical operating room and labor/delivery room. In addition to the practical assistance which these service dogs provide to their recipients, they are instrumental in removing many of the social barriers faced by the disabled in today’s society. One recipient, when asked by a reporter what she liked most about her service dog, immediately responded, “My dog makes my wheelchair disappear.”



Although the cost of breeding and training a service dog for 18 months is in excess of \$10,000, all dogs are provided to their recipients without charge. Each dog is also provided with veterinary care for life, at no expense to the recipient. Corporate sponsorships and general donations from the public underwrite all training and operational costs of the organization.

Canine Assistants also sponsors a significant public education program aimed at educating both children and adults about disabilities and the role that service dogs play in society. Representatives of Canine Assistants conduct educational presentations and recreational therapies for schools, hospitals, assisted-living facilities and community organizations throughout Georgia and the rest of the country. With the growing trend towards mainstreaming the disabled in schools and the workplace, it is essential for the public to have the knowledge necessary to understand and accept their individual differences. For more information on Canine Assistants, or to get involved as a volunteer, check out their Web site at www.canineassistants.org or call 770-664-7178.



ALTHOUGH IT MAY APPEAR THAT THE PARENTS, GUARDIANS OR OTHER FAMILY MEMBERS OF THE BENEFICIARY WOULD BE SENSIBLE CANDIDATES TO ASSUME THE OFFICE OF TRUSTEE OF THE SNT, THE LAW IN SOME JURISDICTIONS SPECIFICALLY PRECLUDES SUCH PERSONS FROM SERVING IN THAT CAPACITY.

Georgia Community Trust, which benefits disabled persons who reside within the state.

By contrast, a “third-party” SNT – one that is funded with assets not belonging to the Beneficiary – is not subject to the payback requirement described above. All property remaining in a third-party SNT at the death of the Beneficiary may be distributed to others as the Trust Agreement directs. Thus, it is essential that the assets of third-party SNTs are not commingled with the assets of self-settled SNTs, which would unnecessarily subject the assets of the third-party SNTs to the payback requirement. A further advantage of third-party SNTs is that there is no age limitation or specific disability requirement as with self-settled SNTs, since third-party SNTs are not subject to the federal law that authorizes self-settled SNTs.

Coordination Is Key

A word of caution: after a Supplemental Care SNT is established for a Beneficiary, all future trusts for the benefit of that Beneficiary must also be drafted as Supplemental Care SNTs. A non-qualifying SNT for the Beneficiary, or any outright transfer (such as a gift, bequest or intestate share to which the Beneficiary becomes entitled), will constitute an “available” asset or resource of the Beneficiary for purposes of maintaining his or her eligibility for need-based benefits. This, in turn, has the effect of rendering even a properly drafted Supplemental Care SNT ineffective for the Beneficiary. Therefore, it is imperative to coordinate planning efforts with others who may wish to benefit the Beneficiary of a pre-existing Supplemental Care SNT. In order to facilitate the necessary coordination with the least amount of inconvenience and expense to those others who wish to provide for the Beneficiary, it is helpful to utilize a “stand-by” Supplemental Care SNT, which may serve as a common receptacle for gifts, bequests and other transfers from third

parties for the Beneficiary’s benefit. In this fashion, other donors may simply “incorporate by reference” the provisions of the pre-existing stand-by SNT, and need not arrange to include a full set of SNT provisions in their own wills or other instruments of transfer.

Trustee Considerations

Since the administration of a SNT is highly labor-intensive, the required fiduciary tasks are generally best performed by a professional Trustee, such as a bank or trust company. Although it may appear that the parents, guardians or other family members of the Beneficiary would be sensible candidates to assume the office of Trustee of the SNT, the law in some jurisdictions specifically precludes such persons from serving in that capacity. In many cases, such persons are often the presumptive remainder beneficiaries of the SNT after the death of the Beneficiary; thus, they might be tempted to “skimp” on disbursements for the Beneficiary to help ensure that a larger fund is available after the death of the Beneficiary for distribution to the remaindermen. Using a corporate Trustee avoids this concern, and also ensures that the management of the SNT will not be interrupted by the incapacity or death of individuals who might otherwise serve as Trustees. Selecting an appropriate Trustee is critical to the effectiveness of the SNT, and many variables must be evaluated and considered in this regard, including the prior experience of the proposed Trustee with administering SNTs, and the relevant fee schedule which would apply to the SNT.

Most corporate fiduciaries charge an annual fee of at least one percent of the value of the trust principal under management. This is a comprehensive fee which covers numerous services, including investment advice, tax reporting and fiduciary bookkeeping. However, if the SNT principal is relatively modest, it may not be cost-effective to utilize a

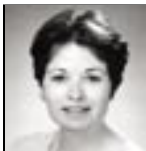
corporate Trustee in the context of a privately administered SNT. In that case, a pooled SNT, such as The Georgia Community Trust, may be a more cost-effective option, albeit one with fewer investment alternatives and other collateral services.

Identifying Qualified Legal Specialists

Even though public demand for SNT planning is clearly on the rise, and increasing numbers of lawyers are choosing to practice in this area, many estate planning attorneys remain unfamiliar with the concept and operation of SNTs. As a result, general practitioners often choose to associate as “co-counsel” an attorney who is proficient in SNT planning when such specialized expertise is needed. State Bar associations may serve as a good starting point for identifying attorneys who have particular expertise in SNT planning. Professional organizations, such as the National Academy of Elder Law Attorneys, may also be of assistance in identifying local attorneys who specialize in this emerging area of law.

The Future Is Bright

Persons with disabilities, and their concerned families, no longer need to contemplate a grim future with limited options. There is at long last a heightened public awareness of the many planning options available to secure the future of persons with disabilities. This, coupled with the swelling ranks of professional advisors able to render competent advice in this emerging area of law, bodes well for the disabled population and those who endeavor tirelessly to provide the best care for them. ♦



Kristen Lewis Denzinger is Of Counsel in the Tax Law Practice Group at Smith, Gambrell & Russell, LLP.
kgrice-denzinger@sgrlaw.com



BRAIN INJURY ASSOCIATION OF GEORGIA

Leading the struggle to improve the lives of those who have survived brain injury, the Brain Injury Association of Georgia (BIAG) works together with injured persons and their families, friends and caregivers to provide support services, advocacy and education on the leading cause of death and disability in children and young adults: Traumatic Brain Injury (TBI). Six times more people experience TBI each year than spinal cord injury, multiple sclerosis, HIV/AIDS and breast cancer combined. A nonprofit foundation dedicated to providing the educational and practical support needed by the families of those suffering from TBI, BIAG is developing an online “Virtual Resource Center” to afford ready access to essential information regarding brain injury issues. This innovative project, funded by a generous grant from The UPS Foundation, will assist injured persons and their families in making the numerous critical decisions they will encounter in the aftermath of a brain injury. Issues covered will include:

- ➔ Medical conditions and intervention;
- ➔ Emotional and behavioral assistance;
- ➔ Transportation;
- ➔ Finances;
- ➔ Legal services (including the use of Special Needs Trusts);
- ➔ Social and recreational services;
- ➔ Educational and vocational services;
- ➔ Physical and mental impairments;
- ➔ Housing; and
- ➔ Advocacy and support groups.

Contributors to this repository of information include doctors, lawyers and other allied professionals with years of experience addressing brain injury issues. BIAG’s Virtual Resource Center will serve as a lifeline for injured persons and their families as they re-order their lives to accommodate a brain injury, and achieve optimal recovery, independence and re-integration into community life. For more information on BIAG, the development of the Virtual Resource Center, or BIAG’s numerous other programs, call 404-603-1477 or visit www.braininjuryga.org.



Large Scale Developments

Working Your Way
Through The Regional
Planning Process



Large-scale developments likely to have effects outside the area in which they are located are often referred to as “Developments of Regional Impact” (DRIs). As a result of a trend towards regional planning, many state and local governments require DRI review “to improve communication among governments on large scale developments and to provide a means of identifying and assessing potential impacts.”¹ More specifically, in many jurisdictions, DRI review is intended to guard against increased pollution, school overcrowding, traffic and other problems associated with large developments.

In Georgia, for example, the following are considered DRIs:

- residential developments containing more than 400 lots or units;
- office developments containing more than 400,000 gross square feet of space; and
- “mixed use” developments containing more than 400,000 total gross square feet of space or covering more than 120 acres.²

Last year, the Georgia Regional Transportation Authority (GRTA) developed regulations for DRI review in Georgia. These regulations took effect January 14, 2002. The interpretation and application of these new regulations continue to raise questions for those affected by the DRI review process, including developers, builders, lenders, lawyers and others.

This article addresses the specific rules in Georgia, especially in counties which do not comply with federal clean air requirements, as a case study of the complex and demanding DRI review process. Other jurisdictions follow similar procedures, and the agency responsible for DRI review in that county or city should be contacted for a complete list of their rules and regulations.³

What Should I Do if I Think My Development Might Be a DRI?

Determining whether a development qualifies as a DRI is generally left to local administrative agencies. Once an Applicant (industry, business or developer) requests official action from a local government, “such as, but not limited to, a



request for rezoning, variance, [land disturbance or building] permit, hookup to a water or sewer system, [and] master or site plan approval (including subdivision),”⁴ the formal DRI review process begins. Applicants generally have little, if any, control over the process since the local governments are required to contact the respective state agencies responsible for DRI review once they receive an application. The municipal or county entity will determine if the development meets certain objective thresholds based upon the size, location or nature of the development. If a development meets the thresholds, then DRI review is mandatory.

In order to assess adequately the amount of time and money a DRI review will require, developers should contact the state agencies responsible for DRI review *before* submitting any type of application to a county or city. While such pre-application is not required, many of the agencies involved in the DRI review process recommend that developers contact them as soon as they know their development likely will have a regional impact. As a practical matter, it is critical to the timing of any transaction to know whether a development requires DRI review. The review may take from four to eight months to complete and some jurisdictions prohibit local governments from taking *any* action prior to DRI approval. Therefore, developments may be delayed as much as one year from the time a permit or similar request is submitted to the local government.

Additionally, DRI review almost always results in the imposition of certain conditions on a development,

such as curb cuts, specific road improvements, pedestrian interconnectivity, etc. A prudent developer should know the likely conditions of DRI approval sufficiently early in the planning process to avoid financial surprises during actual development. If a developer files an application with a local government without including conditions of DRI review approval, he may be forced to amend his application or at least face a deferred final action by the local government. For example, as a condition of DRI approval, the GRTA has required developers to commit to certain curb cuts, road improvements and pedestrian walkways, many of which were not included in the site plans submitted to the local government. As a result, developers have been forced to amend applications after the local government began formally reviewing their plans. The requested rezoning, development permit or variance often is deferred an entire zoning cycle or placed at the bottom of the list in the development department as a result of such changes. Therefore, developers should meet with state agencies early in the process to avoid expensive revisions to site plans or delays which could jeopardize the funding of a development.

What Happens if My Development Is a Development of Regional Impact?

Once a local government submits an application to the state agencies responsible for DRI review and the state confirms the existence of the DRI, the formal review process begins. From this point forward, the developer, the local

AS A PRACTICAL MATTER, IT IS CRITICAL TO THE TIMING OF ANY TRANSACTION TO KNOW WHETHER A DEVELOPMENT REQUIRES DRI REVIEW. THE REVIEW MAY TAKE FROM FOUR TO EIGHT MONTHS TO COMPLETE AND SOME JURISDICTIONS PROHIBIT LOCAL GOVERNMENTS FROM TAKING ANY ACTION PRIOR TO DRI APPROVAL.

government and the various state agencies are on a strict timeline for completion of their review. The following chronology is a synopsis of the DRI review process in Georgia:

1. The Applicant schedules a “methodology meeting” with the GRTA and the regional development center (RDC) assigned to the particular development to discuss the data which will be needed to review the development and to decide upon the format(s) in which these agencies want to see that data. DRI review virtually always requires the Applicant to submit a highly technical report which includes a myriad of traffic and demographic data. The Applicant should hire a qualified traffic engineer and a statistician, at a minimum, to prepare the technical report and attend the “methodology meeting.” The Applicant should also plan to attend the methodology meeting along with any attorneys, engineers, planners or other consultants who may have information regarding the project or who will be involved with its approval.
2. The state agencies responsible for DRI review next hold a joint pre-review conference with: (a) various state administrative agencies who may have input regarding the potential effects of the development; (b) the local government that received the request for official action from the Applicant; and (c) the Applicant. The purpose of the meeting is to determine what data has already been provided and what additional information is needed to start the review. That information includes anticipated traffic generation, environmental impacts, employment and population information, tax consequences and other sophisticated projections related to the effects of the development.
3. Once the state agencies receive all of the information requested at the pre-review meeting, the local government submits a “formal” request to begin the DRI review process. At this point, the state agencies have 30 to 45 days to review the development, depending upon the DRI review regulations for the particular agency.
4. The state agencies notify potentially affected parties (Georgia Departments of Transportation, Natural Resources, and Community Affairs in all cases) of the review and request comments on the proposed development within 10 days. A staff member from one of Georgia’s RDCs also reviews the proposed development, as does a staff member from the GRTA.
5. If problems with the development are noted by either agency, then they will try to resolve them by drafting conditions to improve the impact of the project. If no significant problems are noted or if the problems are resolved by way of appropriate conditions, the RDC’s director is then authorized to return a finding that the proposed development is “in the best interest of the State,” which signifies that the local government may



take the requested action. The GRTA also will make its own final determination, independent of the RDC's findings, as to whether the development is in the best interest of the state and whether to approve or deny the expenditure of federal or state transportation funds related to the proposed development.⁵ It is only after the GRTA's final determination that the county or city may take action on the development request.

Why Can't I Just File My Application With the Local Government and Skip This Process?

The simple answer is that state and local laws in many jurisdictions require DRI review. In Georgia, if the GRTA finds that a development is not in the best interest of the state and a local government approves the development despite the GRTA's recommendation,⁶ The GRTA is authorized under state law to withhold state and federal funding for land and transportation services. The practical effect of this rule is that most local governments simply will not approve a development over a contrary recommendation of the GRTA or any similar agency which has such authority.

In contrast, some agencies do not have the power to require the local government to adopt their recommendation. Local governments are encouraged to comply with DRI review recommendations and condition their approval on specific concerns outlined by the agencies. However, in some jurisdictions there are no direct penalties either to the local government or the developer for failure to comply with the recommendations.

Finally, depending upon the regulations of your jurisdiction, it may be possible to "opt out" of the review process or proceed through an abbreviated process ("expedited review"). The specific criteria for either opting out or expedited review, however, are quite complicated and require an extensive amount of time and study to justify their use. Jurisdictions generally only offer these exceptions to DRI review when an Applicant makes an impressive showing, via highly technical data, that the development is likely to meet very specific goals and objectives for regional mobility and pollution reduction. Again, the local agencies responsible for DRI review should be contacted for a full list of the rules and regulations for expedited review.⁷

How Long Will This Review Process Take?

By regulation, the maximum time allowed for review of a DRI by one of Georgia's RDCs is 45 days, and the GRTA must complete its review not more than 30 days *after* the RDC makes its final determination. However, experience confirms that the process is more likely to take at least four to six months. In order to ensure that the GRTA meets the timelines outlined in its regulations, it is critical to attend the pre-application and methodology meetings referenced earlier to discuss the proposed scope of review. Multiple methodology meetings often occur over the course of several months and each meeting usually takes between three and four hours. Developers must also allow their experts ample time to collect the data required for the technical report.

THE BULK OF THE EXPENSE OF A DRI REVIEW RELATES TO TRAFFIC ENGINEERS, STATISTICIANS EXPERIENCED IN ANALYZING DEMOGRAPHICS OF AN AREA AND AIR QUALITY EXPERTS. THESE FEES MAY RANGE FROM \$10,000 TO \$80,000 PER DRI.

Finally, developers must go through the approval process, as dictated by state and local law, to secure the approval requested (rezoning, development permit, variance, etc.) This post-DRI process also is likely to take at least an additional three to four months, depending on the jurisdiction.

How Much Will the Entire Process Cost?

It depends. While there is no fee to file the Initial DRI Information Form, developers will need to spend substantial sums of money to provide information for the DRI review process. The bulk of the expense relates to traffic engineers, statisticians experienced in analyzing demographics of an area and air quality experts.⁸ These fees may range from \$10,000 to \$80,000 per DRI. The GRTA has developed a highly technical report, the Transportation and Air Quality Analysis (TAQA), that developers need to submit if their development qualifies for complete review. The TAQA includes a detailed report summarizing trip generations produced by the development, air quality analysis and other technical data. Developers undoubtedly will need to hire outside consulting firms to produce the TAQA and the price will depend upon a number of factors including location of the development, availability of qualified analysts to produce the reports and the availability of existing data.

In short, just when you thought it was safe to pull your permit, the DRI process has reared its head to delay its issuance considerably. Careful advanced planning is key to keeping the development on schedule and on budget. ♦

ENDNOTES

- ¹ www.atlantaregional.com/qualitygrowth/reviews/dri.html.
- ² Developers should consult the state or local agency within their jurisdiction responsible for DRI review to determine the thresholds for their particular development. It also should be noted that this list is by no means exhaustive; a multitude of large-scale proposed uses may trigger the DRI process.
- ³ See Florida Department of Community Affairs Regulations, Chapter 28-24; Florida Statute §380.06; see also www.ecfrpc.org/drisummary.html for a discussion of Florida's DRI regulations.
- ⁴ Georgia Department of Community Affairs Regulation 110-12-3-.04(1).
- ⁵ See Endnote 1.
- ⁶ A local government can overturn the GRTA's denial if three-fourths of the local governing body vote to overrule the GRTA's decision to disallow funding. However, it is unlikely that a local government will provide such a ruling.
- ⁷ See Policies and Procedures for Georgia Regional Transportation Authority DRI Review, §3-102.
- ⁸ Developers should consult with the local agency responsible for DRI review in their region to determine if there is any additional data which may require additional experts and fees.



Kathy Zickert is a Partner in the Zoning and Land Use Practice Group at Smith, Gambrell & Russell, LLP.

kmzickert@sgrlaw.com



Linda Dunlavy is Of Counsel in the Zoning and Land Use Practice Group at Smith, Gambrell & Russell, LLP.

lidunlavy@sgrlaw.com



Stephen Fusco is an Associate in the Zoning and Land Use Practice Group at Smith, Gambrell & Russell, LLP.

sffusco@sgrlaw.com

Enron.
Tyco.
Adelphia.
ImClone.
WorldCom.
Global Crossing.

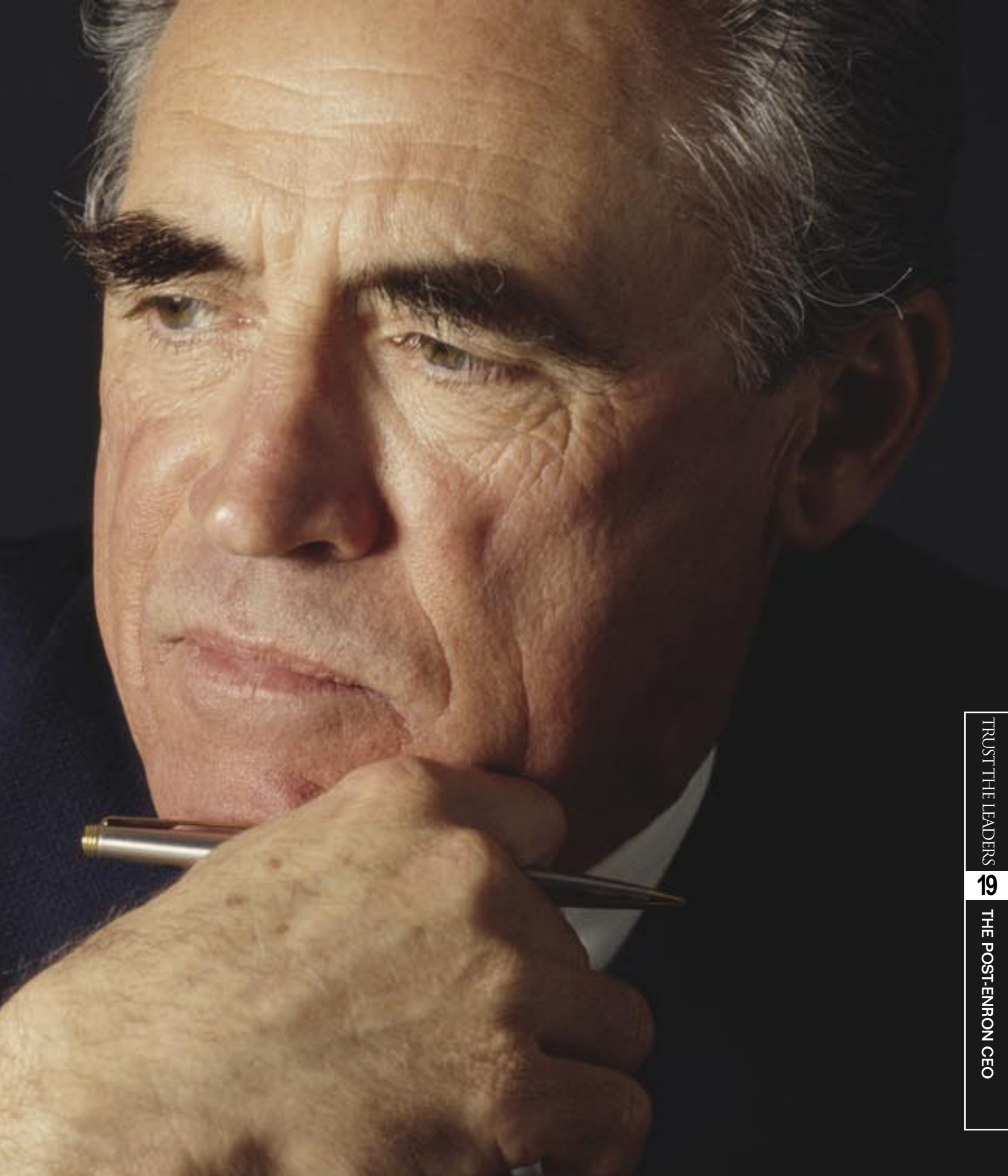
During the past year, Americans have been bombarded with stories of corporate malfeasance at these and other companies on an unprecedented scale. Revelations of widespread accounting shenanigans designed to deceive investors and regulators have created a crisis of confidence in corporate America that played a significant role in a breathtaking decline and then prolonged malaise in the U.S. stock market. These high-profile corporate scandals have also included revelations of deception and greed in the executive suite that turned relatively unknown CEOs Jeffrey Skilling, Bernard Ebbers and Dennis Kozlowski into household names and generated an intense focus on the duties and responsibilities of chief executive officers.

From the ruins of these scandals emerged a sweeping series of new laws and regulations designed to prevent future similar scandals and restore public confidence, placing most of the burden squarely on the shoulders of CEOs. The new rules raise the bar for corporate accountability and place a new emphasis on companies and their executives abiding by enhanced corporate governance standards and procedures. Although the new rules are exceptionally broad and impact many aspects of business, some of the more significant provisions focus on accounting and public reporting, requiring, among other things, that CEOs personally vouch for their companies' financial statements and public reports. Newly expanded criminal penalties significantly increase the stakes for CEOs who turn a blind eye toward discharging their financial and accounting oversight and disclosure duties. In the bright light of the post-Enron business environment, the long list of CEO responsibilities has grown even longer.

The Post-Enron CEO:

BY MARLON STARR & JACOB FRENKEL

It's Lonely At The Top



TRUST THE LEADERS



THE POST-ENRON CEO

AMONG THE DISASTROUS RESULTS OF THESE SCANDALS WERE THE LARGEST BANKRUPTCIES IN HISTORY, PUBLIC DISMAY AT THE DECEPTION, DERELICTION OF DUTY AND OBSCENE GREED IN THE EXECUTIVE SUITE, THE LOSS OF A VAST AMOUNT OF MARKET VALUE OF PUBLIC SECURITIES AND AN OVERARCHING LOSS OF CONFIDENCE IN THE U.S. MARKETS.

The Rise and Fall

As public company CEOs guided their firms during the stock market bubble of the late 1990s, they faced relentless pressure to grow at unsustainable rates, meet the earnings expectations of Wall Street research analysts and further increase the lofty stock prices to which they and their shareholders had grown accustomed. In too many cases, companies resorted to overly aggressive or even deceptive accounting techniques to help them reach their goals, typically creating the appearance of revenues or earnings that did not exist, or concealing significant liabilities or expenses that did. The failure of accounting standards and guidance to keep pace with the technology boom also created a void for some of the now-fallen mighty to exploit. While stock prices soared, CEOs and other top executives reaped enormous financial rewards, primarily through large salaries and even larger bonuses and stock option grants, but also on occasion through low- or no-interest personal loans that boards of directors frequently forgave, sometimes even unknowingly.

The bursting of the stock market bubble in early 2000 and the slowing of the U.S. economy later that year and into 2001 were events that fed upon themselves, worsening both and exposing to the world the accounting chicanery and flimsy financial structures

that had supported some popular companies (Enron, WorldCom, Tyco, Global Crossing and others) and even entire industries (technology, telecommunications). Most recently, the public has been shocked by the details of the egregious financial excess displayed by some CEOs, often while their companies' stock prices sank to new lows, landing those CEOs on the current list of public villains. Among the disastrous results of these scandals were the largest bankruptcies in history, public dismay at the deception, dereliction of duty and obscene greed in the executive suite, the loss of a vast amount of market value of public securities and an overarching loss of confidence in the integrity of the U.S. markets and corporate America generally.

The corporate scandals may also have ended the acceleration of a phenomenon that began in the 1980s: the rise of what Harvard University's Rakesh Khurana calls the "charismatic, superstar CEO."¹ Leaders such as Lee Iacocca, Jack Welch and Steve Jobs typified the early superstar CEO phenomenon – flashy self-promoters who achieved celebrity status and developed an almost cult-like following, not only within their own companies, but also in the business press. While they may have set a positive model, others did not follow. As the stock market skyrocketed

in the mid and late '90s, so did the celebrity of many CEOs, aided by the popularity of CNBC and other business-focused television programs that fed the information habit of ever-increasing numbers of individual investors. But also exposed was what Khurana asserts is the downside to the superstar CEOs: "[C]harisma can be blinding. And the consequences of that blindness can be severe." As an illustration, Khurana offers the deification of Jeffrey Skilling at Enron and the "blind obedience" he apparently induced in his followers. In addition to the management team, "Enron's board of directors also bent to the will of its charismatic leader when it agreed to suspend its code of ethics to allow top executives to participate in the off-balance sheet partnerships" that played an integral role in Enron's eventual collapse. According to Khurana, "charismatic leaders reject limits to their scope and authority. They rebel against all checks on their power and dismiss the rules and norms that apply to others. As a result, they can exploit the irrational desires of their followers."

Among the unwitting victims were those who followed the rules and adhered to good corporate governance models. To be sure, CEOs operated the majority of U.S. companies in an entirely appropriate and ethical manner and justifiably enjoyed the largesse of



economic prosperity and the longest bull market in history. But the grievous acts of a few were sufficient to damage the whole and thrust all corporate chief executives under an intense spotlight of scrutiny.

The Legislative Reaction

Lawmakers and regulators shared the outrage of the investing public. As lower-profile but significant securities cases found their way to prosecutors' desks and criminal indictments accompanied the historically more common Securities and Exchange Commission enforcement actions, the United States Sentencing Commission created more severe punishments under the federal sentencing guidelines for white-collar offenses. The SEC, the stock exchanges and ultimately Congress also sought to restore public confidence by enacting sweeping new laws and regulations designed to vastly improve corporate governance, controls, ethics and accountability in public companies. The new rules directly address the bad acts, executive excess and corporate governance shortcomings revealed by the corporate scandals. In the spring and early summer of 2002, the SEC proposed new rules, and the New York Stock Exchange and Nasdaq began the implementation of stringent new listing requirements. But as the stock market continued to falter

during a summer marked by continued revelations of corporate improprieties and accounting irregularities, the White House pressured Congress to act quickly on legislation to address the issues and established a Corporate Fraud Task Force to coordinate criminal enforcement.

At the end of July, Congress passed (almost unanimously) and President Bush quickly signed into law, the Sarbanes-Oxley Act of 2002. This legislation made sweeping changes to the accounting industry and significant, if less sweeping, changes to the public company corporate governance landscape. The President hailed the Act as "the most far-reaching reform of American business practices since the time of FDR." The Act primarily impacts three areas: the accounting industry; corporate disclosure and governance; and criminal punishment. Outside the accounting industry, those most significantly impacted by the Act are public company CEOs. In an effort to prevent the types of abuses and failures that led to the corporate scandals, Congress has charged the CEO with bearing the burden of restoring confidence in American business by personally vouching for the accuracy of the company's financial statements and public reports, and backing it up with his personal assets. Congress seems to have adopted the view that "CEOs got us

into this mess and they're going to have to get us out."

Although most of the Act's provisions apply directly to publicly-traded companies, privately-held companies are impacted as well. Private companies fall under the purview of some of the new rules and, in particular, the applicability of the new criminal penalty enhancements, when, for example, they engage in private placements to raise capital or provide financial statements to banks to secure a loan. In addition, the Act's focus on the accountability of senior management provides excellent guidance to the leaders of any enterprise, public or private, who are ultimately accountable to stakeholders, and likely will become the baseline and benchmark "best practices" in corporate governance, controls and ethics that are more important than ever. While private companies are not required to abide by all provisions of Sarbanes-Oxley, the new rules may well become the standard expected by lenders, credit agencies, private investors and business partners.

Whether in a public or private company, in the post-Enron business environment, the CEO is operating under heightened scrutiny by regulators, shareholders and the general public. Sarbanes-Oxley imposes several new requirements, prohibitions and responsibilities directly on public

company CEOs (and also CFOs) that arose out of the corporate scandals. Among other things, the Act generally prohibits companies from making loans to them; provides for disgorgement of bonuses, stock option gains and stock sale profits from them if their company is required to restate its financial statements as a result of misconduct and material noncompliance with securities laws; prohibits them from selling stock during certain periods; and requires them to report their permitted stock transactions almost immediately.

But perhaps the most significant new burdens Sarbanes-Oxley places on CEOs, and at the heart of Congress' attempt to restore investor and public confidence, are the certifications now required by CEOs and CFOs in companies' public quarterly and annual reports filed with the SEC.

CEO and CFO Certifications Under Sarbanes-Oxley

Following similar proposals by the SEC, and in response to CEO admissions in congressional testimony that they had little awareness of the contents of the SEC reports that they signed and their companies filed, Congress included in the Sarbanes-Oxley Act a requirement that CEOs and CFOs each make two distinct sets of certifications (which are referred to as "Section 906" and "Section 302" certifications) in each Quarterly Report on Form 10-Q and Annual Report on Form 10-K filed with the SEC.

In requiring these certifications, Congress has pushed the CEO into a far more active and detailed role in the preparation of the company's financial statements and SEC reports than CEOs

Section 906 of Sarbanes-Oxley requires the CEO and CFO to certify that:

- The SEC report "fully complies" with the requirements of the Securities Exchange Act of 1934; and
- The information contained in the report fairly presents, in all material respects, the financial condition and results of operations of the company.

The **Section 302** certifications are much more detailed than the Section 906 certifications and require the CEO to take an active role in the preparation of the SEC report and the company's financial statements in order to make them. The Section 302 certifications require the CEO and CFO to certify that:

- they have reviewed the SEC report;
- based on their knowledge, the report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements in the report not misleading;
- based on their knowledge, the financial statements and other financial information included in the report fairly present in all material respects the financial condition and results of operations of the company;
- they:
 - are responsible for establishing and maintaining disclosure controls and procedures (i.e., controls and procedures designed to ensure that information required to be disclosed by the company in its periodic SEC reports, is recorded, processed, summarized and reported within the required time periods. These controls cover a broader scope of information than just financial information, including developments and risks that pertain to the company's business, such as trend information, and must ensure that such information is accumulated and communicated to management to allow timely decisions regarding required disclosure);
 - have designed such disclosure controls and procedures to ensure that material information is made known to them;
 - have evaluated the effectiveness of the company's disclosure controls and procedures within 90 days of the date of the report; and
 - have presented in the report their conclusions about the effectiveness of the disclosure controls and procedures, based on their evaluation;
- they have disclosed to the auditors and to the audit committee:
 - all significant deficiencies in the design or operation of internal controls (as distinguished from the "disclosure controls," "internal controls" refers to accounting controls used for financial reporting) which could adversely affect the company's ability to record, process, summarize and report financial data, and have identified for the auditors any material weaknesses in internal controls; and
 - any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal controls; and
- they have indicated in the report whether or not there were significant changes in the internal controls or in other factors that could significantly affect the internal controls, since the date of their evaluation, including any actions taken to correct significant deficiencies and material weaknesses.

may have formerly taken, although one that most investors likely always expected of them. In addition, Congress has attached very serious consequences to deliberate misrepresentations by those making the certifications. Although criminal sanctions may result from any deliberate misrepresentation in SEC reports, Sarbanes-Oxley contains specific and severe penalties (fines of

up to \$5 million and prison terms of up to 20 years) for "knowing" or "willful" misrepresentations in the Section 906 certifications. Historically, there have been few criminal prosecutions of CEOs of large U.S. corporations over accounting issues because prosecutors generally would defer to the SEC as the principal enforcer of the federal securities laws. That, too, has changed as prosecutors respond to

WHETHER IN A PUBLIC OR PRIVATE COMPANY, IN THE POST-ENRON BUSINESS ENVIRONMENT, THE CEO IS UNDER HEIGHTENED SCRUTINY BY REGULATORS, SHAREHOLDERS AND THE GENERAL PUBLIC.

congressional and public pressure for federal criminal prosecutions. Where CEOs typically focused on big picture operations and were not part of the paper trail linking executives to a crime, Sarbanes-Oxley facilitates the link.

The CEO's Burden

The detailed certifications required of CEOs by Sarbanes-Oxley (and the serious repercussions of failure in that regard) force CEOs to add a layer of detail to the discharge of their duties that they often did not apply before. A public company CEO must now take a much more active role in the preparation of his company's SEC reports and must have a thorough understanding of the company's accounting policies and the assumptions underlying the preparation of the financial statements. To help CEOs fulfill their obligations, companies should put into place a system of due diligence in the preparation of SEC reports that provides adequate back-up to the certifications required by the CEO and CFO. Most public companies are likely to utilize some form of "sub-certifications" from more junior members of the management team who are responsible for discrete portions of the report. But the likely defense of Messrs. Skilling, Ebbers and Kozlowski that they left it to their subordinates to ensure that the accounting and reporting were proper will no longer fly. While it is not the death knell of delegation, CEOs must now be more circumspect as to what tasks can be appropriately delegated. CEOs now must meet regularly with the CFO, outside accountants and other senior officers working on the financial statements and SEC reports, and ask probing questions to evaluate the process

and ensure accuracy. To do so, CEOs must possess, or quickly develop, an understanding of accounting principles and the application of those principles and various assumptions and estimates in the preparation of financial statements. This can be particularly difficult for CEOs who may have risen from a marketing, sales or legal background as opposed to a finance or accounting background, and who are now required to educate themselves in this area. The CEO must sustain the burdens of self-education and significantly increased involvement in preparing financial statements and SEC reports while continuing to perform the traditional responsibilities of CEOs: planning long-term strategy (by anticipating changes in the company's products, services, distribution channels, clients, technology and competition), motivating personnel, managing the managers, establishing a corporate culture, reporting to the board of directors and dealing with the investment community.

How is the CEO to fulfill his new duties with regard to financial statements and SEC reports while manning the wheel of the corporate ship? Must he now also understand how to repair the ship's engine as opposed to relying on the engine room? The answer is: probably not, but he should know enough to ask the right questions, assess the adequacy of the procedures and bear the ultimate responsibility if it is not done correctly. The bottom line is that it is going to take time. The post-Enron CEO is simply going to have to spend more time at his job than he did previously and employ the "NIFO" method to his increased financial, accounting and

public reporting responsibilities – i.e., "nose in, fingers out."²

Among the internal consequences to CEOs who fail to shoulder this burden is likely to be removal from office by newly empowered, activist boards of directors. The corporate scandals have also awakened corporate boards, which soon must be comprised of a majority of independent, outside directors. Gone are the days of rubber-stamp boards and cozy, wink-wink relationships with management. Post-Enron boards are expected to be strong, independent, active boards, demanding much more from CEOs than in the past. They are also more likely to use a quicker trigger to fire CEOs who don't produce results while meeting their new responsibilities and strictly adhering to the highest ethical standards. Turnover in the ranks of CEOs is likely to increase over the next few years.

The role of the chief financial officer in righting the corporate ship should not be ignored. CFOs face the same criminal penalties as CEOs for material deficiencies in the certifications. But the CFO does not have to leave his comfort zone to the same extent as many CEOs in order to make the certifications and vouch for the financial statements – the CFO typically takes the laboring oar in the preparation of SEC reports. The CFO may take little comfort in that fact, however, when his personal assets and freedom are on the line. But CFOs ought to be thankful for one aspect of the new certification requirements: they ensure that CFOs are not acting alone. Before the new requirements, a CEO like Bernard Ebbers could (and likely will) deny that he was intimately familiar with the

THE LIKELY DEFENSE OF MESSRS. SKILLING, EBBERS AND KOZLOWSKI THAT THEY LEFT IT TO THEIR SUBORDINATES TO ENSURE THAT THE ACCOUNTING AND REPORTING WERE PROPER WILL NO LONGER FLY.

contents of WorldCom's SEC reports because he had no legal obligation to do so, relying instead on the careful work of his subordinates. The certifications now require an appropriately high level of direct involvement and familiarity by the CEO in these matters. If Mr. Ebbers had paid the kind of attention to WorldCom's financial statements and SEC reports now required by Sarbanes-Oxley, it may be less likely that Scott Sullivan (WorldCom's former CFO) would now stand indicted for their alleged shortcomings.

Truth or Consequences

The CEO clearly is faced with a heavy new burden. So what are the new consequences for failures or abuses like those that led to the corporate scandals? The answers lie in two places: the criminal provisions of the Sarbanes-Oxley Act, and, separately, the U.S. Sentencing Guidelines. Many look to the new high-profile criminal penalty provisions of Sarbanes-Oxley with great trepidation, as well they should, where statutory maximum periods of incarceration catapulted from five to 20 and 25 years depending on the offense. While those prison terms have received extensive play in the media, even before passage of Sarbanes-Oxley the U.S.

Sentencing Commission significantly modified its Sentencing Guidelines. The Guidelines apply equally to public and private companies, as well as their respective principals, and now also provide significantly tougher penalties for corporate managers.

The Guidelines have virtually morphed potential halfway house sentences, or four- to five-year stays at Club Fed, to legitimate 15- to 20-year sentences. In fact, many commentators have noted how the effect of the strengthened Guidelines was to create a higher base offense level for the white-collar criminal than for the mid-level armed narcotics trafficker. By shifting covered corporate and securities offenses to the provision governing embezzlement and offenses involving fraud or deceit, a first-time individual defendant could now face imprisonment for a term between 19 and 24 years. The corresponding criminal fine for a corporation, independent of any order of restitution and probation, could be as high as \$290 million under the Guidelines. In fact, the new Guidelines treat large securities fraud more harshly than some street crimes. Against this backdrop, Congress, in Sarbanes-Oxley,

still directed the Sentencing Commission to review the Guidelines applicable to those offenses addressed in the Act to ensure that they adequately reflect the seriousness of the offenses and adequately deter and punish the offenders. Congress specifically directed the Sentencing Commission to review the Guidelines for the offenses of obstruction of justice, fraud endangering the financial security of "a substantial number of victims," and securities and accounting fraud. So, if 19 to 24 years for individuals and \$290 million for corporations are not enough, Sarbanes-Oxley has charged the Sentencing Commission to decide how much more and what else.

In addition to mandating the review and amendment of the federal sentencing guidelines, in Sarbanes-Oxley, Congress also created new federal crimes and increased penalties for existing federal crimes. The titles of the provisions of Sarbanes-Oxley are eye-openers themselves – "Corporate and Criminal Fraud Accountability Act of 2002" (Title VIII), "White-Collar Crime Penalty Enhancement Act of 2002" (Title IX), and "Corporate Fraud Accountability Act of 2002" (Title XI). What some

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Executive Compensation Implications of Sarbanes-Oxley

by Ron Wells

A number of provisions of the Sarbanes-Oxley Act have executive compensation implications for public companies. Most of those provisions were adopted in direct response to the many instances of executive excess that recently have come to light.

Prohibition of Loans to Executive Officers and Directors.

Public companies are now prohibited from extending, arranging for or renewing, either directly or indirectly, any personal loan to any director or executive officer of the company. Loans outstanding on July 30, 2002, are grandfathered, but the loans may not be modified or renewed after that date. While not expressly addressed in the Act, a loan extended after July 30 pursuant to a binding commitment in effect on that date would probably also be grandfathered. The prohibition does not apply to certain loans made by banks, and companies ordinarily engaged in the consumer credit business may continue to provide their directors and officers with certain loans and extensions of credit of a type generally made available by the company to the public and having market terms.

While the Act clearly prohibits certain heretofore common practices and arrangements (e.g., executive relocation loans and accepting an executive officer's promissory note in payment of the exercise price of a stock option), its application in other areas is less clear. Split-dollar insurance is one of those areas. A split-dollar arrangement involving the collateral assignment of the policy to the company to secure the company's right to reimbursement for the premiums paid may be characterized as an extension of credit by the company (in effect, a loan of the premiums paid), and the arrangement would be taxed as a loan under current IRS proposals. On the other hand, a split-dollar arrangement involving an endorsement of the policy to the executive does not have the same loan attributes and would be taxed as the compensatory transfer of an economic benefit to the executive, rather than a loan, under the IRS proposals. However, Sen. Charles Schumer (D-N.Y.), the drafter of this provision of the Act, has indicated that the statutory language was intended to apply to all forms of split-dollar arrangements. If split-dollar arrangements are prohibited, would an arrangement in effect on July 30, 2002, be grandfathered, or would a premium payment after that date constitute a new prohibited loan? Cashless exercise features of stock-option plans constitute another area of uncertainty. Although arguably not the type of arrangements at which the prohibition is aimed, cashless exercise features involving sales of newly issued shares by a broker could be characterized as including a prohibited extension of credit either by the company or by the broker (if arranged by the company). Cashless exercise arrangements in

which the option exercise price is paid through a reduction in the number of shares issued should not be a problem. Guidance from the SEC will be necessary to provide some assurance as to which arrangements are subject to the prohibition and which are beyond the intended scope of the Act.

Forfeiture of Bonuses and Profits. Unless exempted by the SEC, public company CEOs and CFOs will be required to reimburse certain compensation to the company if, as a result of misconduct, the company must restate its financial statements due to material noncompliance with any securities law financial disclosure requirement. The compensation subject to reimbursement includes any bonus or incentive-based or equity-based compensation received from the company during the 12-month period following the initial filing or public issuance of the incorrect financial statement. In addition, those officers will be required to reimburse the company for any profits from the sale of company stock or securities during that 12-month period, without regard to whether the stock or securities had been received from the company as compensation or had been acquired on the open market.

There are currently a number of unanswered questions concerning the scope and practical application of the reimbursement obligation. For example, what type or degree of improper conduct will constitute "misconduct" triggering the reimbursement obligation? There is no definition, but it is clear that the misconduct does not have to be that of the CEO or CFO. Would a stock appreciation right or stock option granted but not exercised during the 12-month period be subject to reimbursement? In that case the executive would not have cashed out to take advantage of any artificial inflation in stock price resulting from the non-compliant financial statements (although the grant of the award may have been made in recognition of the perceived, but artificial, increase in stock value). How about the scheduled vesting during the 12-month period of restricted stock originally granted prior to the issuance of the tainted financial statements? In the case of equity-based compensation, would "reimbursement" take the form of a forfeiture of the applicable equity interest, or could it require a cash payment to the company in an amount equal to the value received by the executive (and if so, how would the value of an option or SAR be determined)?

Prohibition of Trading During Pension Fund Blackout Periods. Effective January 26, 2003, a company's directors and executive officers generally will be prohibited from acquiring or transferring any company equity security (other than an exempted security) during any applicable blackout period under an employee benefit plan if the security was acquired in

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may call the Arthur Andersen obstruction law is Section 802, which amends the obstruction of justice statute by adding two new offenses. One makes it unlawful to knowingly alter or destroy documents with the intent to obstruct or influence any federal investigation or bankruptcy proceeding – the most compelling words in the statute then follow – “or in relation to or contemplation of any such matter or case.” Over time, we will learn a prosecutor’s definition of “contemplation”; meanwhile, the offense is punishable by up to 20 years of imprisonment and/or a fine. The second new offense, aimed at accountants and the destruction of audit records, obligates accountants to maintain corporate audit records or work papers for five years. How do these new offenses impact CEOs? Simply, the collateral effect of this law may be more documents subject to discovery by plaintiffs’ class action lawyers, and federal and state, civil and criminal, investigators.

Sarbanes-Oxley also amends the mail fraud statute to add a specific section relating to securities fraud. It is now a violation of the mail fraud statute to “knowingly execute, or attempt to execute, a scheme or artifice (1) to defraud any person in connection with any security of an issuer...” or “(2) to obtain, by means of false or fraudulent pretenses, representations, or premises,

any money or property in connection with the purchase or sale of any security of an issuer....” The amended mail fraud statute eliminates the purchase or sale element in Section 10(b) of the Securities Exchange Act of 1934 and simply requires that a person “defraud” the victim. With a 25-year maximum prison term and/or a fine and fewer proof elements, federal prosecutors have an important new tool to use against executives of public and private companies in connection with, among other things, capital-raising activities.

In addition to creating new crimes, Sarbanes-Oxley also significantly toughens the consequences for violations of existing crimes. The Act increases the maximum jail term for actual, attempted or conspiracy to commit mail and/or wire fraud from five to 20 years. The Act amends the obstruction of justice statute to make it a crime to corruptly alter, destroy or conceal a document with the intent to impair the object’s integrity or availability for use in an official proceeding or otherwise obstruct any official proceeding. The offense, and an attempt to commit obstruction, now carries a potential penalty of 20 years of imprisonment and/or a fine. More specific to public companies, the Act increases the maximum penalties for violations of the Exchange Act from 10

years of imprisonment or \$1 million, or both, to 20 years of imprisonment or \$5 million, or both. The maximum fine for an entity’s violation of the Exchange Act increased tenfold, from \$2.5 million to \$25 million. Finally, “knowing” or “willful” misrepresentations in the Section 906 Certifications now required by CEOs and CFOs in quarterly and annual reports are punishable by up to 20 years of imprisonment and/or a \$5 million fine.

As if the significantly increased responsibilities now placed on CEOs weren’t difficult enough, the consequences of failure to meet those responsibilities makes the CEO’s task that much more daunting.

Will Coping Be That Bad?

Perhaps in the post-Enron, post-bubble environment, coping with this additional layer of CEO responsibility may not be as difficult as it seems at first blush. Some of the bubble-era motivations that led to the scandals and placed CEOs into this predicament in the first place have abated somewhat. Investors’ expectations are now tempered with a dose of reality – after two (likely three) years of losses, many experts expect annual stock market returns in the 5% to 8% range over the next decade, a major retrenchment from the heady days of 20%

THE POST-ENRON CEO MUST RETURN, TO A CERTAIN EXTENT, FROM THE SEXIER WORLD OF LONG-TERM STRATEGIC THINKING TO THE MORE MUNDANE AND FUNDAMENTAL TASK OF ENSURING THE ACCURACY OF FINANCIAL STATEMENTS.

to 35% annual gains of the S&P 500 between 1995 and 1999. Wall Street firms are under investigation by the NASD, the Manhattan District Attorney and the New York State Attorney General for a range of alleged abuses, centered mostly around the activities of their investment banking units and research analysts, including their relationships with CEOs. With the release of these pressure points, which were among those at the roots of the accounting scandals, CEOs may have more time to focus on operations as well as their new responsibilities without these distractions. This is not to suggest that today's investors won't continue to demand exceptional returns on their investments, but in this environment, exceptional returns could be the reward for companies that focus on operational efficiencies, ethical executive behavior, trustworthy financial statements and reports, and steady, not flashy, growth.

Leadership Means Responsibility

The post-Enron CEO carries a heavy burden. He is almost single-handedly charged with restoring public confidence in corporate America that was destroyed in embarrassing, high-profile scandals at some of the nation's leading companies. As if he didn't have enough on his plate already, the post-Enron CEO must play a more active role than ever in the preparation of his company's financial statements and SEC reports. If he is not already, he must become well versed in finance and accounting matters, sufficient to allow him to publicly vouch for his company's financial statements in the face of draconian consequences for failing to do so.

Today's CEO must be very different from his pre-Enron predecessor. The corporate scandals have proved in spades Rakesh Khurana's premise, that the "charismatic, superstar CEO" who developed huge popular followings often did not serve his company and shareholders well. Corporate reform legislation has curbed his power and public outrage may have buried him. The post-Enron CEO must return, to a certain extent, from the sexier world of long-term strategic thinking to the more mundane and fundamental task of ensuring the accuracy of financial statements. His watchwords should be involvement, communication, understanding and honesty, and by employing these, the post-Enron CEO should successfully bear his burden. But it will not be easy in this new era characterized by no tolerance for ignorance and no excuse for inaction. ♦

ENDNOTES

¹ Rakesh Khurana, "The Curse of the Superstar CEO," Harvard Business Review (September 2002).

² Dr. Timothy S. Mescon, Dean, Coles College of Business, Kennesaw State University.



Marlon Starr is a Partner in the Corporate/Securities Law Practice Group at Smith, Gambrell & Russell, LLP.

mstarr@sgrlaw.com



Jacob Frenkel is Of Counsel in the Securities Enforcement and White-Collar Crime Practice Group at Smith, Gambrell & Russell, LLP.

jsfrenkel@sgrlaw.com

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connection with serving as a director or officer of the company. If this prohibition is violated, any profits realized on the transaction are recoverable by the company, and if the company fails or refuses to bring suit to recover those profits, any shareholder may do so on the company's behalf. Advance notices of impending blackout periods generally must be provided to the plan participants, affected directors and officers, and the SEC, with substantial civil penalties being authorized under ERISA if the plan administrator fails to provide the notices to the participants.

The SEC is authorized to issue rules providing appropriate exceptions to the trading prohibition. Those interpretive rules are also needed to clarify a number of areas of uncertainty. For example, the trading prohibition does not apply to an "exempted security," but no definition is provided for that term. In addition, it is not clear whether the prohibition applies only to securities acquired as compensation for services rendered (an interpretation consistent with the meaning of "in connection with the performance of services" for Tax Code Section 83 purposes) or whether securities acquired to comply with a minimum investment requirement would also be affected. Until interpretive regulations are issued, good faith attempts to comply with these provisions will be respected and deemed to constitute compliance.



Ron Wells is a Partner in the Tax Law Practice Group at Smith, Gambrell & Russell, LLP.

rwells@sgrlaw.com

MOVE OVER AIA

THERE'S A NEW STANDARD FORM CONSTRUCTION CONTRACT FOR OWNERS AND DEVELOPERS



Coming this fall, the Associated Owners and Developers (AOD) will release a new standard form construction contract that promises to change dramatically the way the construction industry uses, negotiates and views standard form agreements. Known as the AOD 2002 Standard Form of Agreement Between Owner and Contractor for a Lump Sum (AOD Agreement), the AOD Agreement incorporates lessons learned from the past with a view towards the future. “We took a hard look at the provisions in the other standard agreements, and asked how they could be improved to promote the project and better preserve the interests of the owner,” said Harvey L. Kornbluh, Chairman and CEO of the McLean, Virginia-based AOD. “We then set out to draft an agreement that was concise, plainly written and fundamentally fair to all parties while being innovative and well-supported by legal precedent.”

To oversee the development of the AOD Agreement, AOD formed a contracts committee consisting of key representatives from DuPont, Mercedes-Benz, Intel, Princeton University, Home Depot, Marriott Hotels, Sun International, Flour City International, Marsh, Inc., Clark Construction Group, Tishman Realty & Construction, Georgia-Pacific Corporation, and The Trane Company. Ira Genberg, head of Smith, Gambrell & Russell’s construction law and litigation practice group, served as the committee’s chair and led the drafting effort.

The result is an equitable, comprehensive agreement that provides common-sense solutions to issues typically encountered on construction projects. Key features include:

- balanced provisions with a unique “success of the project” focus;
- an innovative menu system to customize the agreement; and
- essential terms and general conditions in a single-document format.

LEVELING THE PLAYING FIELD

Before the AOD’s inception, owners and developers lacked a strong, unified national presence. Consequently, they had no meaningful representation in the alliances that produced many of the standard agreements used in the industry. With time, many owners and developers came to believe that those agreements were not always designed to fairly address their interests.

This fact may best be illustrated by the controversial decision of the American Institute of Architects (AIA), in tandem with the Associated General Contractors of America (AGC), to include a mutual waiver of consequential damages in its standard form agreement, AIA Document A201-1997. The AGC did the same for its family of documents.

To put this in context, claims for construction damages are often broken down into *direct damages* and *consequential damages*. Courts historically had awarded owners consequential damages for delays caused by contractors, usually through liquidated damages. Importantly, consequential damages often represented the only meaningful damages an owner would incur. Courts traditionally did not allow contractors to recover most types of consequential damages.

Both AGC and AIA standard agreements now require both the owner and contractor to waive consequential damages. As a result, the owner's damages are limited to the less meaningful direct damages. The contractor's damages are not proportionally restricted, however. Both AIA and AGC standard agreements give the contractor the right to seek damages for field office overhead, general conditions costs, subcontractor delay costs, labor and material escalations, loss of productivity, and the like. Hence, through a mutual waiver of consequential damages, the owner gives up its chief source

for default. The license is reinstated only after a court or arbitrator determines that the architect was in default.

No matter how egregious the architect's behavior, an owner's unauthorized use of the plans before or during the pendency of the arbitration or litigation likely will infringe the architect's copyright and subject the owner to damages. As a result, the owner must shut down the project, infringe the architect's copyright, or attempt to resolve the dispute with the architect who is holding the plans hostage.

Many owners believe that an architect's interests can be adequately protected without revoking the license to use the plans. Returning the parties' focus to the project, AOD recommends that the architect grant the owner a limited, non-revocable license. If the owner is in default, the architect still can recover monetary damages and perfect his lien rights, irrespective of the architect's copyright, allowing the architect to protect his right to payment without significantly impacting the project.

Seeking a fair balance of interests, the AOD Agreement gives more weight to the interests of the project than the interests of any particular party. "Each provision was drafted to promote the project's success, while balancing the interests of the parties," said Kornbluh.

of damages. The contractor does not. The contractor merely foregoes something it traditionally had not been allowed to recover while maintaining a significant avenue of recovery.

The AOD Agreement aims to resolve these types of inequities. In the instance above, the AOD agreement gives the parties control over the treatment of consequential damages. Through a menu of choices, the parties can decide between provisions providing for no waiver, a mutual waiver, or a unilateral waiver of consequential damages. The parties also may include consequential damages in a liquidated damages provision, irrespective of whether they choose to waive or allow consequential damages.

PUTTING THE PROJECT FIRST

Seeking a fair balance of interests, the AOD Agreement gives more weight to the interests of the project than the interests of any particular party. "Each provision was drafted to promote the project's success, while balancing the interests of the parties," said Kornbluh.

The AOD's focus on the all-around success of the project represents an innovative departure from the self-serving ideology of some conventional standard agreements. For example, AIA Document B141-1997 revokes the owner's license to use the architect's plans if the architect is terminated

GENERAL INNOVATIONS The Menu System

The AOD Agreement's menu system represents an innovative approach to contract drafting. Early in the process, the AOD Agreement's drafters recognized that a truly superlative standard agreement must be flexible enough to meet the needs of the parties and the project, yet comprehensive in scope. To achieve this result, AOD added a menu system that provides users with a choice between alternate provisions for some of the more commonly negotiated and modified contract terms. Reducing the use of nonstandard language and the time spent negotiating terms, the menu system allows the user to review several alternate provisions, and select the provision that best suits the user and the project. The menu system also provides a default if no particular provision is selected.

Menu choices cover such common topics as:

- dispute resolution;
- damages;
- waiver of damages;
- claims procedure;
- time of performance;
- document review;
- retainage; and
- indemnification.

DEMANDING A SEAT AT THE TABLE

Professional and trade organizations like the American Institute of Architects (AIA) and the Associated General Contractors of America (AGC) have shaped the standard form agreements predominantly used in the construction industry. Well organized and funded, these groups also effectively promote the interests of their members. Traditionally, owners and developers lacked a similar, unified voice.

That is, until the formation of the Associated Owners & Developers (AOD). Organized in 1994, the group has brought together construction owners and developers, and provided a forum through which they can share information, monitor trends and speak out collectively on issues relevant to their businesses. “In the past, owners and developers as a unit were unrepresented at the construction industry table. AOD sought to change that,” says Harvey Kornbluh, AOD’s Chairman and CEO.

After a number of successful years, the group is ready to roll out its first standard form construction agreement, the AOD 2002 Standard Form of Agreement Between Owner and Contractor for a Lump Sum. Kornbluh promises that others will follow shortly. “AOD’s lump-sum agreement is the first in a line of standard agreements AOD believes will change the way the construction industry does business.”

For more information on Associated Owners & Developers, visit the Construction Channel Web site at www.constructionchannel.net and click on Associated Owners & Developers .

Single Document

The AOD Agreement offers a second, simple improvement over traditional forms: it is a single document. AOD found that the two-document system – agreement and general conditions – tends to create confusion and conflict. For example, it is not uncommon for one or both parties to a standard agreement to fail to realize that the agreement they signed incorporated a second, separate set of general conditions or for a party to add language to one document without realizing that the same issue is addressed by the other. The AOD Agreement’s single document system sidesteps these and related problems altogether.

SPECIFIC ADVANTAGES TO THE AOD AGREEMENT Managing Claims

Many owners believe that existing standard agreements have weak notice and claims procedures. These procedures typically foster misunderstandings, ignore the possibility of mitigation, and delay resolution of claims. For example, AGC Document No. 200 requires “prompt written notice to the Owner of the cause of [any] delays after the Contractor first recognizes the delay.” This provision provides little guidance since it fails to specify when notice is “prompt” and provides no objective standard to determine when the contractor “first recognizes” a delay.

Similarly, AIA Document A201-1997 requires the initiation of a claim within 21 days of the occurrence of the event or the claimant’s first knowledge of the condition giving rise to the claim, whichever is later. The contractor is not obligated to actually make the claim or provide essential facts relating to the claim within any particular time.

These procedures breed adversity and misunderstanding because claims are often made too late to avoid, mitigate or monitor their impact. The claimant believes it is entitled to reimbursement for costs already incurred while the non-claimant believes it was denied an opportunity to investigate the claim and decide how best to manage it.

The AOD Agreement provides a clear procedure for making claims when they occur, requiring early and full disclosure of all facts relating to such claims, cooperation among the parties to avoid or mitigate the impacts of a claim, and prompt resolution of all claims. Processing claims as they arise allows for a more focused and accurate evaluation of the claim’s merits. As a result, the parties treat the claim as a common enemy to conquer rather than a question of entitlement, making it easier to mitigate or resolve the issue before it grows out of control.

Claims for Force Majeure Events

Traditionally, neither party could recover damages for delays caused by events outside their control (i.e., *force majeure*) because, by definition, a *force majeure* event is a delay not attributable to either party. Some current standard form agreements have altered this conventional approach, however.

For example, AGC Document No. 200 now provides that the owner is responsible for paying the contractor's actual costs, without fee, for any "delay in the progress of the Work caused by adverse weather conditions not reasonably anticipated, fire, unusual transportation delays, general labor disputes impacting the Project but not specifically related to the Worksite, governmental agencies, or unavoidable accidents or circumstances..."

The AOD believes that this new approach is unfair; the owner should not be required to pay for delays that are beyond its control or fault, costs not ordinarily covered by insurance. To remedy this inequity, the AOD Agreement offers a rational solution by providing the contractor with a time extension but no money damages in the event that the work is delayed by a *force majeure* event.

Contractor's Use of Payments

The success of any project depends to a large extent upon the proper and timely disbursement of payments to those furnishing labor and materials. Delays in payment can result in abandonment of work, decreased productivity, increased claims, substandard work, and liens. Late payments also may damage the reputation of both the owner and contractor in the community where the project is located.

Many in the industry believe that the standard agreements being used today do not adequately ensure proper and timely disbursement of payments to subcontractors and materialmen. For instance, AIA Document A201-1997 permits commingling of funds, delayed disbursements and unresolved liens. AGC Document No. 200 addresses liens, but fails to include any time period for making payments to subcontractors.

The AOD Agreement reflects the belief that the project benefits significantly when payments are promptly made to all participants. Thus, the AOD Agreement requires that, absent good cause, the owner pay the contractor within an agreed-upon time and that the contractor pay its subcontractors within seven days thereafter.

Additionally, the AOD Agreement requires that the contractor hold payments in trust for the benefit of subcontractors, keeping funds identifiable to ensure that they will be used to satisfy project obligations before any other purpose. Although the AOD Agreement stops short of

requiring contractors to segregate funds, this trust approach is designed to afford added protection to subcontractors in the event of a contractor's bankruptcy.

Finally, the AOD Agreement provides a procedure that allows an owner to withhold payment from the contractor and, upon notice to the contractor, to pay subcontractors by direct or joint payment if the contractor becomes unwilling or unable to make timely and proper subcontractor payments.

Separate Contractors

Projects where multiple prime contractors join forces are becoming more commonplace, and for good reason. This arrangement often allows a project to be completed faster through the combined efforts of several prime contractors who individually may lack the size or expertise to perform the entire scope of work alone. Disputes between the owner's separate contractors can arise, however, due to lack of coordination, congestion and many other factors.

To address this common problem, the AOD Agreement departs from conventional standard form agreements by providing for direct arbitration between the separate contractors. Now, one contractor can resolve a dispute with another without involving the owner.

A NEW STANDARD FOR THE 21ST CENTURY

The AOD Agreement promises to offer an innovative solution to those in the construction industry who believe that the focus of a construction contract should be on the project, rather than the individual team members. Kornbluh has no doubt that it will be well-received. "For the past several years, AOD has worked hard to create a unique agreement that balances the interests of everyone in the construction process. Our organization firmly believes that the construction industry will soon see the AOD Agreement as advanced, effective and fair, and embrace it as an important new standard." ♦



Ira Genberg is a Partner in the Construction Law and Litigation Practice Group at Smith, Gambrell & Russell, LLP.

igenberg@sgrlaw.com



Den Webb is an Associate in the Construction Law and Litigation Practice Group at Smith, Gambrell & Russell, LLP.

djwebb@sgrlaw.com



Scott Cahalan is an Associate in the Construction Law and Litigation Practice Group at Smith, Gambrell & Russell, LLP.

scahalan@sgrlaw.com

EUROPEAN DATA PRIVACY: Beware Of The Pitfalls

Until fairly recently, concern over data privacy has been a relatively low-profile issue among businesses that have come to rely increasingly on new forms of electronic communications and methods of conducting business and storing data via electronic means. Yet in terms of their significance to businesses and consumers and the breadth of their many applications, data privacy issues and the diverse laws and regulations that have arisen to address related concerns impact in some fashion virtually every business. Among the areas where U.S. businesses may unintentionally but nevertheless routinely run afoul of such privacy concerns is compliance with the European Union's (EU) Directive on Data Privacy (the Privacy Directive). This article provides an overview of the EU's Privacy Directive and alternatives to compliance, including the Safe Harbor adopted by the U.S. Department of Commerce.

BACKGROUND

In 1995, the European Commission, the governing body of the EU, adopted the Privacy Directive, which required the 15 member states of the EU (Member States) to bring their laws into conformity with the terms of the Privacy Directive by late 1998. The Privacy Directive is not self-implementing, however, and even though the principles set forth in the Privacy Directive apply in all of the Member States, each Member State will have its own specific implementing legislation which may vary somewhat between Member States. As of the date of this article, all but three Member States (France, Ireland and Luxembourg) have implemented the Privacy Directive. This factor considerably complicates compliance with the individual requirements of each Member State.

APPLICABILITY AND GENERAL REQUIREMENTS

Scope. The Privacy Directive is intended to have broad application. The Privacy Directive requires a “controller” of “personal data” to protect the rights of natural persons with respect to the “processing” of that personal data. Any person or entity that determines the purposes and means of the processing of personal data is deemed to be a controller. For example, an employer would in many cases be a controller with respect to personal data about its employees. Similarly, a company might be a controller of personal data concerning its clients or trading partners and their respective personnel. Moreover, while the increased use of electronic communications and storage systems has heightened data privacy concerns, the scope of personal data protected by the Privacy Directive encompasses data processed or stored using either manually processed offline means or automatically processed online (electronic) means.

The Privacy Directive directs Member States to apply their own implementing legislation to the processing of personal information when a company processing personal data is located within that Member State or when the company makes use of equipment located within that Member State, even if the company is not located within the Member State. For example, a Web site operated in the United States that places electronic “cookies” on the computer of a visitor to the Web site who resides in the United Kingdom would be subject to the implementing legislation of the United Kingdom.

The Privacy Directive has potential application to any United States organization that receives information that can identify an individual in the EU, whether such information is obtained from customers, employees or any other source. Although the Privacy Directive does not apply to the processing of all personal data, such as personal data processed concerning national security or processed for purely personal or household activity, organizations should seek legal advice as to any intended use of personal data in a specific Member State before assuming that the particular use is exempt from the Privacy Directive.

The consequences of failing to comply with the Privacy Directive vary by Member State. Most Member States provide significant civil and criminal monetary penalties and other legal sanctions for violations, even those resulting from mere negligence in not adhering to the Privacy Directive.

More severely, in some Member States officers and employees of a non-compliant company may face personal criminal liability for failure to comply with the Privacy Directive.

General Requirements. Understanding the Privacy Directive’s requirements requires patience – and perhaps an ample supply of aspirin. A company handling personal data must ensure that the data collected is accurate and that the company has a mechanism in place to update and correct inaccurate data. Data must be processed fairly and lawfully and collected and used only for specific, explicit and legitimate purposes. The Privacy Directive also requires that the data be relevant and not excessive for the purpose for which it is processed and that it be kept for no longer than is necessary.

A guiding principle behind the Privacy Directive is that persons whose personal data is being handled must give their consent to such handling. The general rule is that a company may process personal data only if the affected person has unambiguously consented after being adequately informed about the proposed handling of the data. Thus, for instance, a U.S. company with a location in one or more of the 15 EU countries or otherwise doing business in Europe will need to address this requirement for existing and new employees in order to appropriately handle most human resources data. Exceptions (such as where processing is required by law) to the general rule that mandates consent of the person involved are very limited.

In addition, certain categories of personal data that are regarded as being especially sensitive are subject to further restrictions. Among the categories of such sensitive data are information about social or ethnic origin, political opinions, religious or political beliefs, trade-union membership and health data. Again, knowing consent is required to be obtained, but only if the Member State does not prohibit such consent as a matter of public policy.

Determining what constitutes acceptable consent has its own challenges. For transfers of data outside a Member State, special consent rules apply. The Working Party, which is an advisory panel established by the Privacy Directive, has indicated that the consent is not valid if a person is not informed of the particular risks involved with transfer of his or her personal data to a country not providing an adequate level of protection. Consent also is not valid in this situation if the person only gives implied consent (e.g., the person is informed of the transfer of his or her personal data and has not objected to such transfer).



Obtaining consent is only one of the obligations required under the Privacy Directive of a company collecting personal data for processing. Data subjects must also be made aware of the purposes for which the data is collected and be allowed to access and to correct personal data. A company collecting personal data must also implement specified technical and organizational measures to protect personal data from loss, misuse and unauthorized access or disclosure. If a designee, such as an outside service bureau – called a “processor” under the Privacy Directive – carries out the processing of personal data, there must be a written agreement in place with the processor to process data only in accordance with instructions from the controlling company and only in accordance with the terms of the Privacy Directive. Special reporting requirements to the proper supervisory authority within the applicable Member State must also be complied with.

Data privacy issues and the diverse laws and regulations that have arisen to address related concerns impact in some fashion virtually every business.

TRANSFER OF DATA OUTSIDE THE EU

The Privacy Directive requires that any transfer of personal data for processing from a Member State to a non-Member State country, such as the United States, may take place only if that country provides an “adequate level of protection” for the privacy of the transferred data. If a company is located in a country that does not otherwise meet the “adequate level of protection” standard, the company may seek to take advantage of a series of limited exceptions that permit the transfer of personal data to such a country. The three most likely exceptions are consent of the person whose data is transferred (discussed above), inclusion by the company of Commission-approved contractual clauses in applicable business agreements and, in the case of U.S. companies, compliance with the U.S. Safe Harbor framework.

CONTRACTUAL CLAUSES

After several years of extensive discussions and negotiations with interested parties, the European Commission in 2001 adopted two sets of standard contractual clauses for the transfer of personal data to third-party countries. Inclusion

by businesses of these Commission-approved contractual clauses in their applicable contracts will enable the contracts to be deemed to provide an “adequate level of protection” for personal data. Because these clauses may not be readily applicable or adaptable to every contractual situation and their usage may create ambiguities or additional burdens, a company is well advised to evaluate this option for privacy compliance in relation to other available options.

THE U.S. SAFE HARBOR

The Privacy Directive’s “adequate level of protection” standard is somewhat ambiguous. Because of this ambiguity, the U.S. Department of Commerce and the European Commission negotiated a framework, commonly referred to as the Safe Harbor, under which U.S. organizations that comply with this framework will be deemed to provide an “adequate level of protection” in accordance with the Privacy Directive. All Member States are bound by the European Commission’s finding that the Safe Harbor provides an “adequate level of protection.” Therefore, compliance with the Safe Harbor satisfies the diverse privacy requirements of each Member State.

While compliance with the Safe Harbor may not be appropriate in all circumstances, there is a clear trend among U.S. businesses to view the Safe Harbor as the least objectionable manner of complying with the Privacy Directive. The Department of Commerce began accepting Safe Harbor applications in late 2000. As of the date of this article, over 240 companies have been certified under the Safe Harbor, according to the Department of Commerce’s Web site devoted to the Safe Harbor.

To qualify for the Safe Harbor, an eligible United States organization must: (1) adhere to the seven guiding privacy principles set forth in the Safe Harbor (the Principles), and (2) publicly announce its compliance with the Safe Harbor through certification letters filed annually with the Department of Commerce. Compliance with the Safe Harbor may be accomplished through a variety of methods (including developing a qualifying self-regulatory privacy policy or joining an industry self-regulatory privacy program, such as BBBOnline or TRUSTe).

SAFE HARBOR PRINCIPLES

While the Safe Harbor Principles are generally clear, the terminology is slightly at odds with the Privacy Directive (e.g., the Principles use the term “individuals” while the Privacy Directive uses the term “data subject”), which is a potential source of ambiguity in adhering to the Safe Harbor. The seven guiding principles are set forth below.

Compared to the Privacy Directive, the Principles capture the essential protections of the Privacy Directive in a slightly less burdensome form.

Notice. An organization must inform individuals in a clear and conspicuous manner about the purposes for which it collects and uses personal information about them, how to contact the organization with any inquiries or complaints, the types of third parties to which it discloses the personal information, and the choices and means the organization offers individuals for limiting its use and disclosure. This notice must be provided when individuals are first asked to provide personal information to the organization or as soon thereafter as is practicable.

Choice. An organization must offer individuals the opportunity to choose (opt out) whether their personal information is: (a) to be disclosed to a third party; or (b) to be used for a purpose that is incompatible with the purpose(s) for which it was originally collected or subsequently authorized by the individual. Individuals must be provided with clear and conspicuous, readily available, and affordable mechanisms to exercise choice. For sensitive information (i.e., personal information specifying medical or health conditions, racial or ethnic origin, political opinions, religious or philosophical beliefs, trade union membership or information specifying the sexual orientation of the individual), they must be given affirmative or explicit (opt in) choice if the information is to be disclosed to a third party or used for a purpose other than those for which it was originally collected or subsequently authorized by the individual through the exercise of opt-in choice.

Onward Transfer. To disclose information to a third party, organizations must apply the Notice and Choice Principles. Where an organization wishes to transfer information to a third party that is acting as an agent, it may do so if it first either ascertains that the third party subscribes to the Principles or is subject to the Privacy Directive or another adequacy finding or enters into a written agreement with such third party requiring that the third party provide at least the same level of privacy protection as is required by the relevant Principles.

Security. Organizations creating, maintaining, using or disseminating information must take reasonable precautions to protect it from loss, misuse and unauthorized access, disclosure, alteration and destruction.

Data Integrity. Personal information must be relevant for the purposes for which it is to be used. An organization may not process personal data in a way that is incompatible with the purposes for which it has been collected or subsequently authorized by the individual. An

organization should take reasonable steps to ensure that data is reliable for its intended use, and that it is accurate, complete and current.

Access. Individuals must have access to their personal information that an organization holds and be able to correct, amend or delete personal data that is inaccurate.

Enforcement. Effective privacy protection must include mechanisms for ensuring compliance with the Principles, recourse for individuals affected by noncompliance with the Principles, and consequences for the organization when the Principles are not followed. At a minimum, such mechanisms must include: (a) readily available and affordable independent recourse mechanisms by which each individual's complaints and disputes are investigated and resolved by reference to the Principles and damages awarded where provided under applicable law or otherwise; (b) follow-up procedures for verifying that the attestations and assertions made about an organization's privacy practices are true and that privacy practices have been implemented as presented; and (c) obligations to remedy problems arising out of failure to comply with the Principles by an organization announcing its adherence to them and consequences for such an organization. Sanctions must be sufficiently rigorous to ensure compliance by the organization.

FINAL OBSERVATIONS

Seeking expanded business opportunities in Europe has long been an attractive means for growth by U.S. businesses. Doing so, however, now involves considerably more attention to the details of privacy law compliance for most businesses. U.S. businesses will also find that Europe's broad approach to privacy protection is not unique. Other countries, such as Canada and Australia, to name but two, that have large markets focused upon by many U.S. businesses, have also adopted comprehensive laws dealing with data privacy and protection. Because of this, U.S. businesses are well advised to adopt a proactive approach to confirming the existence and applicability of data privacy regulations in Europe and other countries in which they do business. ♦



Brett Lockwood is a Partner in the Corporate Law Practice Group at Smith, Gambrell & Russell, LLP.

blockwood@sgrlaw.com



Tim Johnson is an Associate in the Corporate Law Practice Group at Smith, Gambrell & Russell, LLP.

tvjohnson@sgrlaw.com



MEET ASCAP: PROTECTING THE MUSIC

Serving as Copyright Counsel to the American Society of Composers, Authors and Publishers

BY JOYCE KLEMMER

For more than 50 years, Smith, Gambrell & Russell has represented the American Society of Composers, Authors and Publishers (ASCAP) in all music copyright infringement cases brought in the state of Georgia. SGR's work with ASCAP began with the work of partner I.T. Cohen, who became Southern General Counsel of ASCAP in 1939. When ASCAP became active in Georgia, Cohen did it all. He would personally investigate bars, restaurants and radio stations to determine if they were playing ACSAP members' music without a license from ASCAP. If they were, Cohen would either license them, or draft a complaint and bring suit against those infringers who refused to take an ASCAP license voluntarily.

What is ASCAP? The American Society of Composers, Authors and Publishers was founded in New York in 1914 and is the oldest performing right licensing organization in the USA. It is the only U.S. performing right organization owned and run by its writer and publisher members. ASCAP was founded so that creators of music could be paid for the public performances of their works and users (licensees) could comply with the federal copyright law.

By the end of the 19th century, the musical stage had become a major form of popular entertainment. Increasing economic value was attached to dramatic performances of music, especially light opera and operettas, the precursors of the uniquely American art form, the musical comedy. Many of these performances were unauthorized performances, however, from which the copyright owner derived no financial return. In response, Congress extended the right of public performance to musical works. The amendment of the copyright law in 1897 provided that any person publicly performing any copyrighted dramatic or musical composition without the consent of the copyright owner would be liable for damages to be assessed at a sum not less than one hundred dollars and potential criminal misdemeanor charges.¹ Prior to the 1897 Amendment, the copyright laws did not grant



a performance right in music; protection was limited to duplications of the work in copies, such as sheet music.² A mechanism was needed to bring music creators and music users together to enforce the performance right.

Europe was far ahead of the United States in developing performing right societies for music. It was recognized that, as a practical matter, it would be impossible for a single copyright owner to determine who was performing his music and to take the necessary steps to license them or protect his rights through lawsuits for infringement. On the other hand, even law-abiding users of music would find it equally impossible to find the owner of the copyrighted composition and negotiate an individual license with him.

To solve these problems, collective licensing organizations, termed performing right societies, were formed in many countries. The first such society was formed in France in 1851. The principal goal was to enable the writers and publishers of music to license all nondramatic public performances of their works, and to serve as a clearinghouse for music users. By means of a blanket license, the user is able, in one transaction, to obtain the right to perform all works of all members of the domestic society as well as works of affiliated foreign societies, without burdensome and costly administrative and record-keeping requirements.

ABOUT JOINING ASCAP

You can join ASCAP as a writer, a publisher or both if you meet the eligibility requirements. To become a writer member you must be the writer or co-writer of a musical composition or a song that has been commercially recorded, or performed publicly, or performed in any audiovisual or electronic medium or published and available for sale or rental. Publisher applicants must contact an ASCAP membership office. Further information about joining ASCAP can be found on their Web site at www.ascap.com/about/howjoin.



It wasn't until 1910 that the idea of forming an American society was proposed by the Italian opera composer Giacomo Puccini. He told his American publisher, George Maxwell, of the role played by the Italian performing right society. Maxwell discussed the idea with his lawyer, Nathan Burkan. In October 1913, eight writers and publishers and Burkan met in Luchow's Restaurant in New York City and agreed to form the American Society of Composers, Authors and Publishers – ASCAP. Others, including Irving Berlin and John Philip Sousa, joined ASCAP as soon as it was formed.³

All members of ASCAP grant it the nonexclusive right to license nondramatic public performances of their works. The members authorize ASCAP to bring suit in their name against infringers and appoint ASCAP attorney-in-fact to conduct and resolve such suits. ASCAP collects royalties from bars, restaurants, radio stations, television networks and stations and, more recently, Internet music providers, among many other entities, and pays royalties to its members.

Under the blanket license, users pay only a single annual license fee to ASCAP for their right to use any and all of the members' musical works and the works of members of affiliate societies throughout the world. Licensees do not have to account separately and pay for each work performed. Complete information on the schedule of fees is readily available from any ASCAP licensing office, and from the main office in New York City. Information is also available on ASCAP's Web site, www.ascap.com.

ASCAP currently has approximately 140,000 writer and publisher members. Among many others, members of

AMERICAN COMPOSERS FORUM

In addition to representing ASCAP, SGR is also representing the Atlanta Chapter of the American Composers Forum in licensing a CD that was created by two of its composer members and two Atlanta Boys & Girls Clubs. With the help of its funder, The Arthur M. Blank Family Foundation, the Atlanta Chapter's RE-MIX Program gave members of two Atlanta Boys & Girls Clubs the chance to find out exactly what it takes to create and record a CD. The Program was the Chapter's after-school initiative and its first collaboration with Boys & Girls Clubs. It also represented the first composer residency for Boys & Girls Clubs of Metro Atlanta, an organization that has provided after-school programs and facilities since 1938.

For more information about the success of the program, go to The American Composers Forum's Web site at www.composersforum.org.

ASCAP include Stevie Wonder, Bruce Springsteen, Kenny Loggins, Hal David and Burt Bacharach, Wynton Marsalis, Quincy Jones, Diane Warren, Lionel Richie, Rod Stewart and Madonna. ASCAP's members also include the successors to the estates of legendary composers and lyricists such as Aaron Copland, Morton Gould, George and Ira Gershwin, Richard Rodgers and Oscar Hammerstein, II, Cole Porter and Henry Mancini. ASCAP participates in a wide range of music industry concerns, including sponsoring events, fostering the development of new talent, and supporting music-related philanthropic activities through The ASCAP Foundation. ♦

ENDNOTES

- ¹ Korman and Koenigsberg, *Performing Rights in Music and Performing Right Societies*. Journal of the Copyright Society of the USA, Vol. 33, No. 4, July 1986 at p. 348.
- ² Id. at 336; Act of January 6, 1897, Ch. 4, 29 Stat. 481 (the "1897 Amendment").
- ³ HUBBELL, THE STORY OF ASCAP (Unpublished Memoir); Waters, Victor Hurbert, A LIFE IN MUSIC (1955), 433 – 34.



Joyce Klemmer is a Partner in the Intellectual Property Law Practice Group at Smith, Gambrell & Russell, LLP.

jklemmer@sgrlaw.com

Finland & SGR:

An International Partnership

When you think of Finland, what is the first thing that comes to mind? Is it Helsinki, home of the 1975 Helsinki Accords on human rights and site of the Bush/Gorbachev and Clinton/Yeltsin summits of the 1990s? Is it the elegant Finnish flag – a blue cross on a white background – fluttering over the memorable Olympic performances of Paavo Nurmi, better known as “the Flying Finn,” and Lasse Viren, who fell in the finals of the 10,000 meters in Munich in 1972 but got up and went on to win the gold medal in world-record time?

Perhaps your first thought was not of Finland as a leader in global industry. And yet some of the world’s leading firms in telecommunications, including Nokia, call Finland “*koti*,” or “home.” Interestingly, there are more Finnish companies located in Georgia than in any other U.S. state. As a result, Smith, Gambrell & Russell has, for more than 25 years, enjoyed the unique opportunity of representing a variety of Finnish companies in their U.S. operations.

SGR first represented Nokia, headquartered in Espoo, in the mid-1970s when, as the Nokia representatives tell it, SGR partner John Saunders was the only lawyer in Atlanta they found who knew that Finland was not still part of Russia. “In the early days, when we would describe our Finnish practice, the response most often heard was, ‘Did you say Finland?’” recalls Saunders. “Now that Finnish companies are at the forefront of leading industries, no one asks that question anymore.”

SGR attorneys have represented a wide variety of Finnish companies in matters in the United States such as complex litigation involving sophisticated power installations; contract disputes growing out of paper mill equipment sales and applications; acquisitions, including registration of American Depositary Receipts with the SEC; and the patent prosecution, immigration, real estate and similar transactions associated with most inbound foreign investment.

One of the most rewarding aspects of SGR’s Finnish connection is that many of the firm’s attorneys have enjoyed the opportunity to travel to Finland, which Saunders, who has visited Finland more than 30 times, describes as “beautiful and energetic.” Litigation partner Rex Lamb fondly recalls a February visit with Saunders and a Finnish client to Lapland, the northernmost region of Finland, in celebration of the successful close of a business transaction. Highlighting the trip



was a two-day snowmobile safari 100 miles north of the Arctic Circle. Rex, who “required” regular doses of Finnish vodka to combat the freezing weather, remembers that the client leading the expedition declared the trip a success “because everyone survived.”

SGR has been happy to return the favor, and has hosted numerous Finnish clients and dignitaries, including the current Prime Minister of Finland, Paavo Lipponen, and two former Prime Ministers. In the last two months alone, SGR has hosted more than 40 representatives of Finnish businesses.

In recognition of his work with Finnish companies, John Saunders was appointed the Honorary Consul of Finland for the State of Georgia in 1996. In that capacity, John represents Finland in Georgia and as a member of the Atlanta Consular Corps.

Smith, Gambrell & Russell is proud of its affiliation with the Republic of Finland. Finnish flags are displayed prominently throughout the office; Finnish chocolates are served along with Finlandia vodka at firm receptions; and books on Finnish history are readily available.

The firm looks forward to continuing its relationship with Finland, which SGR’s attorneys have found to be enriching and rewarding both personally and professionally, and hopes for Finland and its people a future as bright as the Finnish midnight sun.



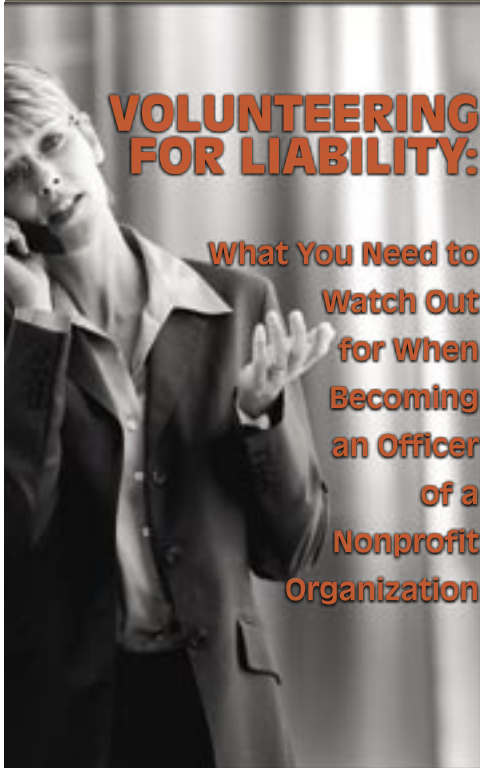
Dana Richens is a Partner in the Litigation Practice Group at Smith, Gambrell & Russell, LLP.

drichens@sgrlaw.com



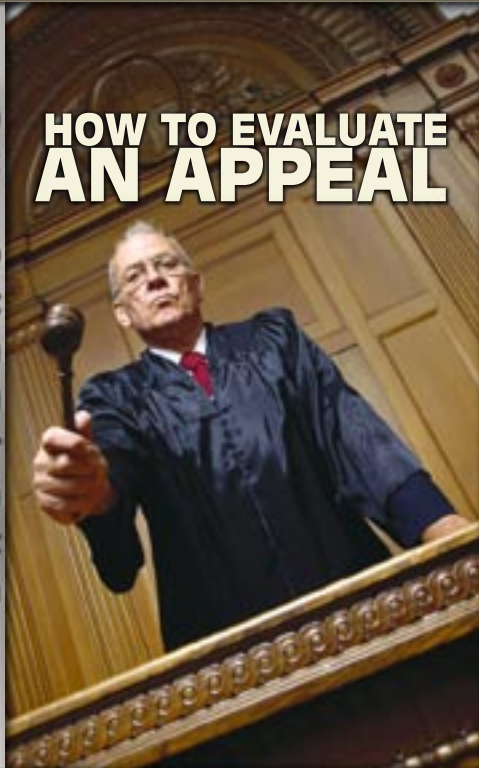
Tamara Mosashvili-Shevardnadze is an Associate in the International Law Practice Group at Smith, Gambrell & Russell, LLP.

tmosashvili-shevardnadze@sgrlaw.com



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