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COMPLIANCE PROGRAMS

The Justice Department Intensifies Its Focus On Corporate Compliance and Ethics Programs

BY STEVEN A. LAUER

Since the Clinton Administration, the Department of Justice (Department) has issued guidance to the offices of the U.S. Attorneys throughout the nation on the review and assessment of corporate compliance and ethics programs.[1] That review and assessment was intended to enable those prosecuting officials to determine whether and how to prosecute organizational defendants for violations of federal law. In those memoranda, the guidance of which was incorporated in 2008 as Chapter 9 of the U.S. Attorneys' Manual,[2] the Department expressed the principles by which prosecutions should be considered in respect of business organizations:

> Where a decision is made to charge a corporation, it does not necessarily follow that individual directors, officers, employees, or shareholders should not also be charged. Prosecution of a corporation is not a substitute for the prosecution of criminally culpable individuals within or without the corporation. Because a corporation can act only through individuals, imposition of individual criminal liability may provide the strongest deterrent against future corporate wrongdoing. Only rarely should provable individual culpability not be pursued, particularly if it relates to high-level corporate officers, even in the face of an offer of a corporate guilty plea or some other disposition of the charges against the corporation.[3]

Thus, while clearly establishing its policy for pursuing organizations for their misconduct, the Department reserved in that provision its prerogative to prosecute individuals for illegal corporate conduct. Nonetheless, the focus in its day-to-day activities in pursuit of that policy seemed to be on securing redress for violations of federal law, even securing many agreements for the payment of damages without admissions of liability by the organizations and without prosecutions of individu-

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[1] That advice was expressed in a series of memoranda issued by successive Deputy Attorneys General and other officers of the Department. The most recent complete expression of how Department personnel should assess possible criminal charges against business organizations was contained in a memorandum issued by Deputy Attorney General Mark Filip on Aug. 28, 2008 (http://www.justice.gov/sites/default/files/dag/legacy/2008/11/03/dag-memo-08282008.pdf) (Filip Memorandum).

[2] References to that guidance herein will be in the form "USAM § 9-___."

[3] U.S. Attorneys' Manual § 9-28.200.

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als. Much criticism of the Department centered around that perceived dearth of prosecution of individuals for their companies' acts despite the quoted language.[4]

On Sept. 9, the Department issued a memorandum to clarify and stress its policy in respect of ''individual accountability for corporate wrongdoing'' by amending some provisions on the general guidance on the subject as contained in the U.S. Attorneys' Manual. According to that memorandum, ''[o]ne of the most effective ways to combat corporate misconduct is by seeking accountability from the individuals who perpetrated the wrongdoing.''[5] This clarification of policy introduces clarity into the Department's policy, but it also creates challenges for corporate compliance and ethics programs.

The Yates Memorandum and Other Related Actions of the Justice Department

The Yates Memorandum sets out ''six key steps to strengthen [the Department's] pursuit of individual corporate wrongdoing.'' Of those six steps, one relates most directly to how corporate compliance and ethics programs operate (the others constitute direction to Department employees and officials and only indirectly affect business organizations in that they might affect the form of the scrutiny to which those organizations find themselves subject).

The step in question is this: ''in order to qualify for any cooperation credit, corporations must provide to the Department all relevant facts relating to the individuals responsible for the misconduct.''[6] This step will affect much of the content of Chapter 9 of the U.S. Attorneys' Manual that has served as guidance for the design and implementation of corporate compliance and ethics programs.

For example, § 9-28.700 states that ''[i]n gauging the extent of the corporation's cooperation, the prosecutor may consider, among other things, whether the corporation made a voluntary and timely disclosure, and the corporation's willingness to provide relevant information and evidence and identify relevant actors within and outside the corporation, including senior executives.'' That permissive language (''may consider . . . willingness . . .'') seems to have been replaced by a mandatory directive, for the Yates Memorandum expands on the language quoted at footnote 6 as follows:

> to be eligible for any credit for cooperation, the company must identify all individuals involved in or responsible for the misconduct at issue, regardless of their position, status or seniority, and provide to the Department all facts relating to that misconduct. If a company seeking cooperation credit declines to learn of such facts or to provide the Department with complete factual information about individual wrongdoers, its cooperation will not be considered a mitigating factor pursuant to USAM [§] 9-28.700 et seq.[7]

The Department expects its attorneys, when investigating possible violations of federal law, to ''strive to obtain from the company as much information as possible about responsible individuals before resolving the corporate case.'' Yates Memorandum, p. 4.

Soon after releasing the Yates Memorandum, the Department announced the appointment in its Fraud Section of its first ''compliance counsel.''[8] The responsibilities of that position identified by the Department when it announced that step included the following:

- (1) ''provid[ing] expert guidance to . . . prosecutors as they consider the enumerated factors in the United States Attorneys' Manual concerning the prosecution of business entities, including the existence and effectiveness of any compliance program'';
- (2) whether the corporation has taken meaningful remedial action, such as the implementation of new compliance measures to detect and prevent future wrongdoing'';
- (3) to ''help prosecutors develop appropriate benchmarks for evaluating corporate compliance and remedial measures''; and
- (4) to ''provide expert guidance to help prosecutors and monitors evaluate whether the implementation of such measures is effective and in keeping with the terms and purposes of Fraud Section resolutions'' of charges.

The head of the Department's Criminal Division expanded on those responsibilities in a presentation contemporaneous with the appointment. The compliance counsel will ''help [prosecutors] evaluate each compliance program on a case-by-case basis—just as the department always has—but with a more expert eye.''[9]

The Yates Memorandum, the appointment of a compliance counsel within the ranks of the Department and the additional detail expressed by the Criminal Division regarding the standards by which compliance programs would be assessed by the Department, taken together, represent a more nuanced and focused examination of compliance programs.

Implications for Corporate Compliance and Ethics Programs

Chief compliance officers and other corporate officials involved with their companies' compliance and ethics programs should understand the implications of the guidance contained in the Yates Memorandum, for those implications may be considerable in effect. First,

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[4] See, for example, the criticism of a settlement with General Motors quoted in Ivory and Vlasic, $900 Million Penalty for G.M.'s Deadly Defect Leaves Many Cold, *The New York Times*, Sept. 18, p. B1 (http://www.nytimes.com/2015/09/18/business/gm-to-pay-us-900-million-over-ignition-switch-flaw.html): '' 'This outcome fails to require adequate and explicit admission of criminal culpability from G.M. and individual criminal actions,' said senators Richard Blumenthal of Connecticut and Edward J. Markey of Massachusetts, both Democrats, in a joint statement. 'This outcome is extremely disappointing.' ''

[5] Memorandum entitled ''Individual Accountability for Corporate Wrongdoing'' issued Sept. 9, under the signature of Deputy Attorney General Sally Quillian Yates, p. 1 (Yates Memorandum) (13 CARE 1952, 9/11/15).

[6] *Ibid.*

[7] Yates Memorandum, p. 3.

[8] See ''New Compliance Counsel Expert Retained By The DOJ Fraud Section'' (press release dated as of Nov. 5), posted at http://www.justice.gov/criminal-fraud/file/790236/download (60 CARE 60, 11/3/15).

[9] ''Assistant Attorney General Leslie R. Caldwell Speaks at SIFMA Compliance and Legal Society New York Regional Seminar, '' posted at http://www.justice.gov/opa/speech/assistant-attorney-general-leslie-r-caldwell-speaks-sifma-compliance-and-legal-society (39 CARE, 10/2/15).

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that guidance crystallizes the divergent interests of the entity and its employees and agents. Second, the Department's standards for considering whether and the extent to which it will recognize a company's compliance and ethics program as a mitigating factor in the charging decision will put a premium (even more than it has in the past) on the collaboration between the organization's compliance and ethics program and its law department (assuming that those functions are distinct within the organization).

Organizational interest versus personal interest

In-house lawyers have long struggled with the implications for their practices that arise from the fact that they represent the entity rather than individual employees, even senior executives.[10] To the extent an employee believes that the company's attorney (whether in-house counsel or an outside lawyer) does not represent his/her interests, that employee, in the context of an internal investigation, or in a deposition, trial testimony or otherwise, likely will be on guard and less forthcoming with counsel. Corporate counsel thus seek to assuage an employee's concerns in that regard so as to secure the maximum cooperation (and accurate information) with minimal resistance.

The Yates Memorandum makes it clear that the interests of the company and its employees diverge from the inception of an investigation (if not sooner). In that memorandum, the Department stated that ''[t]he requirement that companies cooperate completely as to individuals, ***within the bounds of the law and legal privileges***, *see* USAM § § 9-28.700 to 9-28.760, does not mean that Department attorneys should wait for the company to deliver the information about individual wrongdoers and then merely accept what companies provide. To the contrary, Department attorneys should be proactively investigating individuals at every step of the process—before, during, and after any corporate cooperation.''[11] The Department had earlier stressed (in the memorandum issued in 2008) that the attorney-client privilege and the attorney-work-product doctrine, which it recognized and did not intend to override through its review of corporate compliance programs, do not shield the information uncovered during an investigation.

What the government seeks and needs to advance its legitimate (indeed, essential) law enforcement mission is not waiver of those protections, but rather the facts known to the corporation about the putative criminal misconduct under review.[12]

Thus, while recognizing the continuing vitality of legal privileges, the Yates Memorandum makes it clear that the Department will look to the company under investigation to provide information regarding its employees' possible criminal conduct in order even to qualify for any cooperation credit. The company will need to weigh its interest in securing credit for cooperating with a federal investigation against its need to preserve from disclosure any materials protected by the attorney-client privilege or the attorney-work-product privilege. When it makes that assessment, however, the employee's own interests need not (and, in the view of the Department, should not) appear in the calculus.

Since in-house attorneys must view their organizational employers as their clients, those employers' interest in securing credit for cooperating thus puts them at odds with their employees. This could very well lead to further challenges in managing internal investigations, since much of the information subject to such an investigation must come from employees, and companies typically expect and rely on their employees' forthrightness in those investigations.[13]

The need for compliance and legal to collaborate and cooperate fully

Compliance and law departments often occupy distinct and separate positions in a corporate structure. In other organizations, they co-exist, with compliance reporting to or residing within a corporate law department. Regardless of the structure (and without addressing whether either structural approach serves the organization better[14]), for effective compliance, the two

[10] The duty of an in-house lawyer is owed to his/her corporate employer, but it often leads to challenges when individual employees are deposed or testify in that employer's litigation. For example, an in-house attorney in California advised an employee of the company that employed that in-house attorney that the attorney was that employee's attorney for purposes of a deposition of that employee. When that employee was later terminated for his testimony in that deposition, he claimed that the company's in-house attorney committed malpractice and breach of a fiduciary duty owed to the deposed employee. The state appellate court ruled that the terminated employee raised triable issues regarding his relationship with that attorney, which could establish an attorney-client relationship that would support his claims for breach and malpractice: *Yanez v. Plummer*, 221 Cal. App. 4th 180 (2013), http://corporate.findlaw.com/litigation-disputes/in-house-counsel-represent-employee-risk-malpractice.html. The general rule is that: ''The attorney does not (and cannot) represent any of the officers, directors or employees of the corporation as individuals with respect to their corporate activities if their interests are different from the corporation.'' Attorney Client Privilege in the Corporate Setting: How To Keep Your Confidential Information Confidential—A Guide for Corporate Clients (Pennsylvania Bar Association In-House Counsel Committee, https://www.pabar.org/public/committees/in-house/pubs/inhouseguide.asp.

[11] Yates Memorandum, p. 4 (emphasis added).

[12] Filip Memorandum, pp. 8-9.

[13] In a speech delivered on Nov. 16, the author of the Yates Memorandum acknowledged that the changes announced in that memorandum accentuate the conflict between the interests of an individual employee and the organization in a way that could make internal investigations more challenging (69 CARE, 11/17/15). ''I will acknowledge that our focus on culpable individuals may make some employees nervous. Some may have reason to be nervous. But to the extent that there's a tension between the interests of the company and the interests of individuals in an internal investigation, that dynamic is nothing new. This tension is reflected in the admonition that corporate counsel give employees that they represent the company not the employee and that the company may provide to the government any information that the employee provides.'' Deputy Attorney General Sally Quillian Yates Delivers Remarks at American Banking Association and American Bar Association Money Laundering Enforcement Conference, posted at http://www.justice.gov/opa/speech/deputy-attorney-general-sally-quillian-yates-delivers-remarks-american-banking-0.

[14] At least some regulators believe that the compliance function should exist independent of and not report to the legal function: ''The OIG believes it is generally not advisable for the compliance function to be subordinate to the . . . general counsel, or comptroller or similar financial officer. Separation of the compliance function helps to ensure independent and objective legal reviews and financial analysis of the company's

functions must coordinate their activities well and communicate so as to effectively cover all issues that might arise to ensure the organization's compliance with those mandates that impact its operations, whether those mandates issue from governmental sources or otherwise.

Some commentators have opined that, on account of the Yates Memorandum, ''the board [of directors] is well advised to direct the general counsel to lead the organizational response to the new DOJ initiatives. The general counsel would then be expected to work collaboratively and cooperatively with the chief compliance officer, as a valued organizational partner.''[15] While that may be good advice for matters that have come to the attention of federal officials and triggered a governmental investigation or worse, corporate officers know that the compliance department's range of responsibilities is much broader than that. For example, issues might come into the compliance department through a variety of mechanisms, such as:

- (1) through a hotline report received by telephone or via e-mail,
- (2) a letter received in the compliance department, the health and safety department, the human resources department or another corporate office,
- (3) an in-person complaint lodged in any of a number of locations throughout the organization, or even
- (4) by means of a ''complaint box'' (or similarly designated channel).[16]

Many hotline complaints do not raise any issues requiring legal review and action and are handled solely within the compliance department with no involvement of lawyers.[17] Many others may not, on an initial review, raise issues that implicate legal potential legal risk for the company but the investigation undertaken by the compliance personnel may reveal the existence of legal risk. Unfortunately, at the time a report arrives in the compliance department, the personnel likely will not be able to predict with assurance whether it will trigger a law department investigation or other steps.

At that stage, of course, the company's lawyers cannot take the lead in handling the matter. Until a legal issue within the scope of the report is recognized, compliance personnel will manage the investigation and response.

If a hotline report[18] does raise one or more issues that implicate possible legal exposure for the organization, the compliance personnel will need to transfer the investigation to the company's lawyers in some fashion.

The transfer from compliance to legal personnel must be done properly and carefully. The fruits of the investigation should not be lost or overlooked, but the lawyers' prerogative to pursue any inquiry that seems relevant to them in respect of the legal issues will override the compliance findings themselves. Moreover, the applicability of privilege to any investigation by and the other activities of the company's lawyers must be assured.[19]

Even short of a full transfer of a matter to the company's lawyers, close coordination between compliance personnel and the company's lawyers is necessary. In the course of investigating a hotline report, compliance personnel may need advice from the lawyers as to the proper means of conducting that inquiry or answers to questions that arise in the course of the inquiry.

Thus, the personnel involved in a company's compliance and ethics initiatives, whether they are housed in a compliance department or a law department or both, may have to treat all but the most inconsequential issues as potential government investigations, because the downside of not doing so may be too dire. This means close coordination between those two corporate functions to ensure that the corporate response is most effective and most believed.

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compliance efforts and activities.'' Department of Health and Human Services Office of Inspector General, OIG Compliance Program Guidance for Pharmaceutical Manufacturers, 68 Fed. Reg. 23731, 23743 n. 13 (2003).

[15] Peregrine, ''New DOJ Actions Impact GC and Compliance Officer Roles—What Should the Board Do?'' *Corporate Counsel Magazine* (Oct. 20), posted at http://www.corpcounsel.com/id=1202740253741?keywords=michael+peregrine&publication=CC+Corporate+Counsel.

[16] The Network (a company that provides outsourced corporate whistle-blowing hotline services) reports the following data regarding the means by which reports come to the attention of its client companies in 2014: 78.1 percent were received by telephone, 21.1 percent via a Web-based mechanism, 0.7 percent by e-mail and none by faxed report. ''2015 Corporate Governance and Compliance Hotline Benchmarking Report,'' p. 14.

[17] The Department recognizes the role of compliance personnel in handling many compliance-related reports with no processing by lawyers or others. In remarks prepared for an industry compliance conference, the head of the Department's Criminal Division stated that compliance personnel ''are often the first line of defense against money laundering and other financial crimes. . . . Well before a grand jury subpoena is served or a witness is interviewed, compliance officers . . . can and do step in and stop issues from becoming problems down the road.'' Assistant Attorney General Leslie R. Caldwell Speaks at SIFMA Compliance and Legal Society New York Regional Seminar, note 9 *supra* (60 CARE 60, 11/3/15). The author of the Yates Memorandum also stressed the importance of robust compliance programs in recent remarks. ''At DOJ, we ... want to restore and help protect the corporate culture of responsibility. That's only possible with strong compliance programs—and with rigorous internal controls that help companies self-assess and self-correct. It is in our mutual interest to ensure that we root out misconduct, promote fairness and demonstrate that no one is above the law.'' Deputy Attorney General Sally Quillian Yates Delivers Remarks at American Banking Association and American Bar Association Money Laundering Enforcement Conference, note 13 *supra*.

[18] I use that term to include a report of some sort of compliance issue or violation regardless of the mechanism by which the report is communicated to the company.

[19] A hotline report submitted to a company originates from a source that is not within the scope of the ''control group'' of an organization (*i.e.*, those officers and other employees entitled to raise with the company's lawyers legal issues via communications that would be subject to the attorney-client privilege) and does not relate to existing or reasonably anticipated litigation (a prerequisite for applicability of the attorney-work-product doctrine), so privilege does not apply to activities of compliance personnel relative to a hotline report. Moreover, because a court probably would consider a compliance program a ''business operation'' rather than a legal operation (certainly when organizationally distinct from a law department), the activities of a compliance department would not be entitled to privilege as a general rule.

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Conclusion

Recent moves by the Department reinforce the need for robust compliance programs. Incorporating the steps announced in the Yates Memorandum to those previously codified in the U.S. Attorneys' Manual, in light of the creation of the compliance counsel position within the Department, leads to an inevitable conclusion:

- federal prosecutors will expect companies to have created such programs as a matter of course;
- those programs will receive added scrutiny when the prosecutors weigh whether to bring charges and, if they do bring charges, how serious the charges should be; and
- the review by prosecutors will be more informed by real-world experience than may have been the case previously.

The substantive changes announced in the Yates Memorandum also create some substantive challenges for compliance personnel. Conducting an internal investigation may prove more difficult in light of the prosecutors' heightened interest in pursuing individual liability for corporate actions and their stated insistence that companies provide ''all relevant facts relating to the individuals responsible for the misconduct.'' How best to conduct such an inquiry in light of those divergent interests, heightened as they will be as a consequence of the policies set out in the Yates Memorandum, must be carefully considered and calibrated.