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The Department of Justice really, really wants you to voluntarily disclose your company's violations. Considerations for GCs and CCOs. (Part II of II)

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OCTOBER 26, 2022

DOJ's mixed signals undermine confidence for voluntary disclosures

Have the expected benefits of voluntary disclosure of potential criminal violations become more clear or more cloudy? In a series of announcements over the last year, culminating in a speech on September 15, 2022, Deputy Attorney General Lisa Monaco rolled out a series of significant changes[1] to federal corporate criminal enforcement policies.

In separate speeches, Assistant Attorney General Kenneth Polite touted DOJ's new corporate enforcement polices, including DOJ's controversial new requirement, in settlements and resolutions with companies, that CCOs certify, *under penalty of criminal prosecution*, "that the company's compliance program is reasonably designed and implemented to detect and prevent violations of the law ... and is functioning effectively." These policies are intended to encourage companies to voluntarily disclose potential offenses and expand their cooperation with federal prosecutors, but will they have the desired effect?

Companies have a powerful and reasonable aversion to voluntary disclosure. GCs, CCOs and Boards know they will thereafter lose virtually all control and predictability over the duration, breadth, and/or expense of the investigation and resolution that will inevitably follow.

Making the case for companies to disclose in the face of this perception requires DOJ to alter the calculus by creating more certainty and specificity as to the expected result. On balance, DOJ's new corporate enforcement policy is positive, but there are reasons to be wary as some of the provisions introduce new concerns that may discourage companies from making a voluntary disclosure.

Below, we will decipher the key elements of the new corporate enforcement policies and identify what actions companies should consider taking in response. We will discuss the policy initiatives in the order of likely significance to in-house counsel.

(1) Attempted clarity on the benefits of voluntary disclosure and cooperation

(2) Additional guidance on how prosecutors will evaluate a company's "history of misconduct"

(3) New guidance encouraging companies to deploy "claw backs" and other measures to remove individual financial incentives to engage in misconduct

(4) Attempted clarity on when compliance monitors will be imposed

(5) Renewed priority on prosecting individuals

The DOJ policy specifically encourages companies to consider the adoption of "claw backs" in compensation agreements.

In Part I,[2] we discussed DOJ's attempts to clarify the expected benefits of voluntary disclosure and how it will evaluate a company's "history of misconduct." Part II will discuss DOJ's intended approach to employee compensation and the use of "claw backs," attempted clarifications about its use of compliance monitors and, finally, its efforts to improve the rate of prosecuting individuals.

1. New guidance encouraging companies to deploy "claw backs" and other measures to remove individual financial incentives to engage in misconduct

By now, General Counsel and CCOs are very familiar with the DOJ Criminal Division's Evaluation of Corporate Compliance Programs.[3] It provided a comprehensive set of considerations that federal prosecutors should utilize in assessing the effectiveness of a company's compliance program both at the time of the offense conduct and at the time of resolution. In this month's policy announcement, DOJ has indicated that it will now include within those previously announced considerations whether and how the company has incentivized employees to act in support of the company culture of ethics and compliance.

Prosecutors are now encouraged to consider whether the company's "compensation systems" enable financial penalties to be

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levied against current or employees who may have contributed to misconduct. The DOJ policy specifically encourages companies to consider the adoption of "claw backs" in compensation agreements. The policy also encourages companies to employ positive financial incentives to reward employees to act in support of or promote compliance within the organization. In a separate speech,[4] AAG Polite announced that the details of this policy will be worked out in the months to come.

Hopefully, future deliberations will lead DOJ to consider the many conflicts with state and foreign employment laws that challenge a company's ability to consistently implement the types of actions DOJ is proposing. We have encountered situations where China-based employees involved in FCPA-related fraud were terminated by the company and the employees succeeded in a subsequent lawsuit to be reinstated.

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Despite the company's good faith efforts to punish the employees, the company eventually had to make significant severance payments merely to separate the wrongdoers from the company. Similar situations have been observed during and since the "Me Too" movement where the employment law protections of employees and the company's ability to terminate them "for cause" are not necessarily aligned with the preference that "wrongdoers not be rewarded."

To advance company culture, companies have separated from toxic leaders, managers, and employees only to later have to overcome employment laws with payments that might be inconsistent with the new guidance. Moreover, CCOs should carefully consider how financial incentives to report compliance issues are structured so as to not unintentionally create *disincentives* for prompt reporting of potential violations. For example, rewarding employees for a plant operating without environmental violations could actually discourage reports by employees.

Non-Disclosure Agreements? Another potentially troubling issue in the policy is that prosecutors are guided to consider the company's use of non-disclosure agreements (NDAs) in compensation and severance agreements and whether they are being used by the company to "inhibit the public disclosure of criminal misconduct by the corporation or its employees."

All GCs and CCOs well know that NDAs are ubiquitous in the modern corporation from sales to engineering and product development to compensation to separation agreements. The failure to obtain an NDA in many contexts leaves the company open to subsequent allegations against it for theft of trade secrets or infringement claims and defamation. It is entirely appropriate for companies to prevent the public disclosure of its operations and/or maintain the privacy of its employees in employment and severance agreements.

The appropriate and necessary use of NDAs has often led large and small companies to deploy "self-serve" NDA tools to reduce the burden on in-house legal departments. An official government policy suggesting that prosecutors interpret the use of non-disclosure agreements as improperly "inhibiting" public disclosure of criminal offenses is worth the attention of GCs and CCOs. This guidance is especially concerning where DOJ successfully employed this argument of "NDA as obstructive tool" in the prosecution of an in-house lawyer and security officer at Uber.[5]

Takeaway: *GCs and CCOs should review their company's use of NDAs in situations where criminal allegations are possible and/or consider including language permitting disclosure in cooperation with official investigations of criminal offenses.*

2. Attempted clarity on when compliance monitors will be imposed

One of the headlines from the initial corporate enforcement policy announcements last fall was that the Biden Administration would substantially increase the frequency with which corporate monitors were imposed in resolutions. Last week, it appeared that the Department was attempting to walk back that impression by first dangling the potential of avoiding a monitorship to companies who self-disclose and then endeavoring to more specifically define the circumstances when a monitor would be required.

Unfortunately, the new policy announcement unnecessarily undermines the goal of providing predictability to companies considering self-disclosure by expressly noting that it was still a discretionary case-by-case decision and then providing a lengthy list of the circumstances in which the Department would nonetheless be more likely to impose a monitor. It is difficult to conceive of a compliance failure that would not meet one or more of the listed aggravating criteria. (e.g., "whether the underlying criminal conduct involved the exploitation of an inadequate compliance program or system of controls.")

While the new policy still makes it difficult to predict when a monitor will *not* be imposed, the new policy does reinforce when it definitely will be imposed. A monitor is very likely to be imposed in situations whenever the weaknesses leading to or enabling the misconduct has not been remediated with appropriate discipline, personnel changes, policy changes and/or process control changes.

Moreover, even if all of these acts of remediation have happened, it seems very clear that a monitor will nonetheless still be imposed if, at the time of resolution, those new process changes have not already been implemented for a reasonable period and the effectiveness of those new controls has not been fully tested and proven to be effective.

Companies seeking to avoid a monitor should be thinking ahead, remediating as soon as possible, and building an evidentiary record of the effectiveness of their controls. In some cases, voluntarily retaining an independent monitor, well before resolution negotiations to verify a company's compliance program can be critical in convincing the government that the issues have been

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resolved, the new controls have been tested over time and the new program is operating effectively. This approach, in our experience, can be beneficial for the company.

The new enforcement policy also committed the Department to important reforms and transparency in how corporate compliance monitors are selected and how their ongoing work is supervised. These changes respond to criticisms of cronyism and favoritism in the pool of applicants and selected monitors and perceptions from companies that monitors are unaccountable and uncontrollable.

3. Renewed priority on prosecuting individuals

The new corporate enforcement policy emphasizes that a company may earn full cooperation credit only if it immediately and continuously provides any incriminating evidence to the Department prosecutors. The policy statement asserts that the Department has been frustrated in holding individuals accountable because some companies seek to delay turning over vital evidence that could have made it possible to prosecute individuals more quickly. It seems reasonable that the Department would judge a company as uncooperative if it had purposefully and unreasonably withheld such evidence. However, we do not see the policy announcement as a real change nor one that will increase the likelihood of individual prosecutions.

Over recent decades, as the Department has obtained criminal resolutions with more and more companies of ever-increasing dollar value, the complaint has arisen that, in those same cases, relatively few, if any, individuals have been held accountable. The Department has been criticized for this and especially when virtually no individual was held accountable for the misconduct that led in the 2008 financial crisis. It has attempted previous policy changes to encourage individual prosecutions.

In September 2015, the Yates Memo[6] sought to delay the related corporate resolution until criminal liability for individuals could be charged or ruled out. But that policy did not lead to an appreciable increase in prosecutions of individuals. Many practitioners observed that the primary result was to delay and slow down corporate resolutions such that they took longer and cost more.

The reality is that prosecutors who want to charge individuals do not need any additional policy motivation to do so. There are fewer prosecutions of individuals than companies because individuals are much harder to prosecute than a company. *Respondeat superior* and other theories of corporate responsibility make it easy to hold companies responsible for the actions of rogue employees and companies are very risk averse and inclined to settle. Consequently, evidence and theories of liability is not as rigorously challenged.

Individuals, in contrast, are often beyond a prosecutors reach and even if they are not, they fight very hard to avoid going to jail. Prosecutors implicitly know that their evidence and theories will need to withstand a tough challenge and tend to only charge cases where they have sufficient confidence that they will meet their burden. The policy change will likely encourage some companies to more aggressively cooperate but it likely will not increase prosecutions of individuals.

Notes

[1] https://bit.ly/3D6J2Zp

[2] https://bit.ly/3gSiflG

[3] https://bit.ly/2YT1DW4, updated June 2020

[4] https://bit.ly/3Fg2qWH

[5] *US. v. Sullivan*

[6] https://bit.ly/3rdoibc

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This article was first published on Westlaw Today on October 26, 2022.

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