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511 - Ethics Issues in Government Investigations

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Faculty Biographies

Jordan Eth

Jordan Eth is co-chair of Morrison & Foerster's Securities Litigation, Enforcement, and White Collar Defense Group. He has represented dozens of public companies and their officers and directors in securities class actions, SEC investigations, derivative suits, and internal investigations.

Prior to joining Morrison & Foerster, Mr. Eth served as a law clerk to the Honorable Chief Judge Robert F. Peckham, United States District Court for the Northern District of California. Prior to that, he worked as an economist in Washington, DC, first for the United States Department of Energy and then for the Budget Committee of the United States House of Representatives.

Mr. Eth has received a California Lawyer Attorney of the Year Award for co-leading the successful defense of JDS Uniphase Corp. and its former executives in a securities class action jury trial seeking \$20 billion in damages. He is a frequent author and speaker on securities litigation topics and actively participates in programs held by The SEC Institute, the Practising Law Institute, and the Stanford Directors' College. He is recommended by Chambers USA, Legal 500, Best Lawyers in America, Benchmark, and PLC Which Lawyer?

Mr. Eth received his BA from Swarthmore College, with highest honors and Phi Beta Kappa. He received his JD from Stanford Law School, was elected to the Order of the Coif, and served as co-president of the Moot Court Board.

Jodie Kelley

Jodie L. Kelley is the vice president and general counsel at the Business Software Alliance. In this role, Ms. Kelley leads BSA's domestic and international anti-piracy programs, its efforts against Internet crime, and its educational programs to promote software license compliance and respect for intellectual property. She serves as BSA's general counsel for all corporate matters and manages BSAs' anti-piracy programs and counsel in Europe, the Middle East, Africa, Asia-Pacific, and the Americas. Representing the largest copyright-based industry, BSA operates in more than 80 countries worldwide.

Prior to joining BSA, Ms. Kelley served for six years as vice president and deputy general counsel of Fannie Mae, a government-sponsored enterprise chartered by Congress to provide liquidity, stability and affordability to the US housing and mortgage markets. There, she was responsible for managing the company's litigation portfolio and its responses to various governmental inquiries. She also was responsible for advising the company on issues including antitrust and anti-fraud. Previously, she was a partner at Jenner & Block in Washington, where she specialized in civil and regulatory litigation

and handled cases before trial and appellate courts and regulatory agencies throughout the country.

Ms. Kelley is a member of the board of directors of the DC Central Kitchen.

She earned her BSS from The Pennsylvania State University and her JD from Harvard Law School.

Monica Palko

Monica J. Palko is vice president, corporate responsibility for ITT Defense & Information Solutions. Ms. Palko has responsibility for leading the design, implementation, and monitoring of a company-wide government contractor compliance program and the defense corporate responsibility program.

Ms. Palko joined ITT from Rosetta Stone Inc., where she served as vice president and associate general counsel. There she handled a broad range of matters, including IP infringement and contracts. She previously served as associate corporate counsel at BearingPoint Inc., where her responsibilities included corporate governance matters such as securities fraud litigation, as well as SEC, DOJ and USAO investigations. Prior to joining BearingPoint, Ms. Palko was a trial attorney in the commercial litigation branch of the United States Department of Justice. She represented the United States in numerous trial and appellate proceedings, including bid protests. Before joining the DOJ, Ms. Palko was an attorney with Bracewell & Patterson LLP (now Bracewell & Giuliani).

Ms. Palko is currently chair of the ACC Litigation Committee.

She received her BA from Hendrix College and her JD from George Washington University Law School.

Paul Pelletier

U.S. Department of Justice, Criminal Division

Jordan Thomas

Jordan A. Thomas is an assistant director in the Division of Enforcement of the U.S. Securities and Exchange Commission. At the SEC, Mr. Thomas has also served as an assistant chief litigation counsel. In these roles, he has investigated and litigated a wide range of high-profile matters including: financial fraud, offering fraud, broker-dealer violations, insider trading, and market manipulation cases. As a special adjunct duty, he serves as the national coordinator for the Division's new cooperation program.

Prior to joining the SEC, Mr. Thomas specialized in large, complex, financial services litigation involving the FDIC and OTS as a trial attorney at the Department of Justice. During college, he also worked as a stockbroker.

He currently serves as a reserve officer in the United States Navy.

Mr. Thomas received a BA from Bennington College and is a graduate of Southwestern University School of Law.

Ethics Issues in Government Investigations
ACC Annual Meeting 2010

How the Whistleblower Provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act and the SEC's Individual Cooperation Policy Affect Your Company

By Jordan Eth and Justin D. Hoogs

I. Overview of Federal Bounty Programs and Cooperation Policies

Over the years, the federal government has created a patchwork of programs offering monetary incentives and protections to individuals who report misconduct to enforcement authorities. The *qui tam* process under the False Claims Act (“FCA”) is the primary example of this type of program.¹ The FCA allows private citizens to (1) file a lawsuit on behalf of the government charging fraud by government contractors, and (2) share up to thirty percent of any damages recovered. Persons who make use of the *qui tam* process are protected by accompanying anti-retaliation provisions. The FCA’s whistleblower bounty model has provided the basis for other programs, including one used by the Internal Revenue Service to reward persons who report tax evasion,² and — until recently — one used by the Securities and Exchange Commission (“SEC”) to reward persons who report insider trading.³

Accompanying the development of federal bounty programs has been an emphasis by regulators and enforcement authorities on companies’ cooperation in government investigations. Cooperation is considered a key factor in analyzing whether and to what extent leniency or credit should be granted to investigated companies. In 2003, the Department of Justice (“DOJ”) adopted the Thompson Memorandum, named for then-Deputy Attorney General Larry Thompson, which made mandatory the use of nine factors by which companies’ cooperation would be assessed in federal criminal investigations.⁴ Before the adoption of the Thompson Memorandum, similar factors existed in formal DOJ policies, but were considered advisory.

In 2006, the Thompson Memorandum was superseded by the McNulty Memorandum, named for then-Deputy Attorney General Paul McNulty, which reaffirmed many of the Thompson Memorandum’s factors, but placed greater restrictions on prosecutors’ ability to request privilege waivers.⁵ In August 2008, the DOJ issued the

¹ See 31 U.S.C. § 3730.

² See 26 U.S.C. § 7623(b).

³ See 15 U.S.C. § 78u-1(e). As discussed in Part II, this program has been repealed and replaced by the Dodd-Frank Act’s whistleblower program.

⁴ U.S. Dep’t of Justice, Memorandum from Deputy Att’y Gen. Larry D. Thompson to Heads of Dep’t Components and U.S. Att’ys, Principles of Fed. Prosecution of Bus. Orgs. (Jan. 20, 2003). The Thompson Memorandum is attached at Appendix A.

⁵ U.S. Dep’t of Justice, Memorandum from Deputy Att’y Gen. Paul J. McNulty to Heads of Dep’t Components and U.S. Att’ys, Principles of Fed. Prosecution of Bus. Orgs. (Dec. 12, 2006). The McNulty Memorandum is attached at Appendix B.

most recent version of the Principles of Federal Prosecution of Business Organizations, which list the factors considered when conducting an investigation, determining whether to bring charges, and negotiating plea agreements.⁶ The Principles modify the McNulty Memorandum by no longer allowing prosecutors to request that companies (1) waive privilege; (2) refrain from advancing attorneys' fees to employees; or (3) refrain from entering into joint-defense agreements.

The SEC issued a Release announcing its own cooperation policy in 2001, when it decided not to pursue an action against the Seaboard Corporation despite evidence that its former controller had caused the company's books and records to be inaccurate and its financial reports misstated.⁷ The SEC took action against the former controller, but did not charge the company, pointing to the "nature of the conduct and the company's responses." In the Release — known as the Seaboard Report — the SEC outlined thirteen factors it considers in determining the extent of a company's cooperation. The SEC updated its standards for imposing civil penalties on corporations in 2006, when it reaffirmed that cooperation is a factor the SEC considers in determining the propriety of a corporate penalty.⁸

In the past year, two significant developments have changed the enforcement landscape and will require companies to reexamine how they design and implement compliance and ethics programs, respond to allegations of misconduct, and decide whether and when to disclose potential misconduct to enforcement authorities. First, the recently-passed Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank" or the "Act") creates powerful incentives and protections for whistleblowers that provide information to the SEC regarding violations of the securities laws.⁹ As noted in the Senate Banking Committee Report, part of the impetus for the creation of the new whistleblower program was the inadequacy of existing programs in meeting enforcement objectives. The Committee cited a recent SEC Office of the Inspector General ("OIG") report indicating that since the inception of the Insider Trading and Securities Fraud Enforcement Act of 1988 whistleblower program, there had been a total of "only seven payouts to five whistleblowers for a meager total of \$159,537."¹⁰ The OIG concluded

⁶ Dep't of Justice, Principles of Fed. Prosecution of Bus. Orgs. (Aug. 2008). The Principles are attached at Appendix C.

⁷ SEC, Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934 and Commission Statement on the Relationship of Cooperation to Agency Enforcement Decisions, Exchange Act Release No. 44969, 76 SEC Docket 220, Accounting and Auditing Enforcement Release No. 1470 (Oct. 23, 2001). The Seaboard Report is attached at Appendix D.

⁸ SEC, Press Release, Statement of the SEC Concerning Financial Penalties (Jan. 4, 2006). The Financial Penalties Statement is attached at Appendix E.

⁹ Dodd-Frank Wall Street Reform and Consumer Protection Act, H.R. 4173, 111th Cong. (2010). The whistleblower provisions of Dodd-Frank are attached at Appendix F.

¹⁰ S. Rep. No. 111-176, at 111 (2010). Days after Dodd-Frank passed, however, the SEC paid a bounty of \$1 million to two individuals who provided information and documents in connection with the successful prosecution and collection of civil penalties in an insider trading case. SEC, Press Release, SEC Charges Pequot Capital Management and CEO Arthur Samberg with Insider Trading (May 27, 2010).

that the SEC's insider trading bounty program "[was] not fundamentally well-designed to be successful."¹¹

Second, in addition to company cooperation, enforcement authorities are now placing a greater emphasis on cooperation by individuals in investigations and related enforcement actions. Earlier this year, the SEC issued a policy statement describing the analytical framework it uses to evaluate cooperation by individuals.¹² The individual cooperation policy complements the whistleblower incentive and protection provisions of Dodd-Frank. The details of both of these developments are discussed below.

II. The Dodd-Frank Act's Whistleblower Provisions and the SEC's Policy Regarding Cooperation By Individuals

A. The Dodd-Frank Act's Whistleblower Provisions

The Dodd-Frank Act is broadly intended to reform the financial regulatory system in response to the recent financial crisis. As part of this reform, the Act creates new provisions intended to encourage whistleblowers to report violations of the securities laws to the SEC. In addition, the Act includes anti-retaliation provisions that enhance existing protections for whistleblowers. Some commentators have referred to the provisions as a "secret weapon" against fraud on Wall Street and in corporate America. Others are more skeptical and question whether the trend toward informant-based law enforcement methods is desirable. The SEC is expected to issue final regulations implementing the changes made by Dodd-Frank by April 2011.

1. The Dodd-Frank Act's Whistleblower Incentive Provisions

As mentioned above, before Dodd-Frank, the SEC's authority to pay bounties to whistleblowers who reported violations of securities laws was limited to cases of insider trading. Under Section 21A(e) of the Securities Exchange Act of 1934 (the "Exchange Act"), the SEC was authorized to award up to ten percent of the civil penalties collected in insider trading cases to whistleblowers who provided information contributing to successful prosecutions. Dodd-Frank amends the Exchange Act by adding Section 21F: Securities Whistleblower Incentives and Protection.¹³ Section 21F repeals Section 21A(e) and *requires* the SEC to reward whistleblowers who voluntarily provide "original information" relating to a violation of the securities laws that results in successful prosecution of specified enforcement actions.

To qualify as "original," the information must be (a) "derived from the independent knowledge or analysis of a whistleblower"; (b) "not known to the [SEC] from any other source, unless the whistleblower is the original source of the

¹¹ H. David Kotz, Inspector General, SEC, Assessment of the SEC's Bounty Program, Report No. 474 (Mar. 29, 2010).

¹² SEC, Policy Statement Concerning Cooperation by Individuals in its Investigations and Related Enforcement Actions, 17 C.F.R. § 202.12, Release No. 34-61340 (Jan. 19, 2010). The Policy Statement Concerning Cooperation by Individuals is attached at Appendix G.

¹³ H.R. 4173, 111th Cong. § 922(a).

information”; and (c) “not exclusively derived from an allegation made in a judicial or administrative hearing, in a governmental report, hearing, audit, or investigation, or from the news media, unless the whistleblower is a source of the information.”¹⁴ Specified enforcement actions include “any judicial or administrative action brought by the [SEC] under the securities laws” resulting in monetary sanctions exceeding \$1 million.¹⁵

The whistleblower is entitled to an award “not less than [ten] percent” and “not more than [thirty] percent” of the monetary sanctions collected in the action and in related actions brought by the Attorney General of the United States, an appropriate regulatory authority, a self-regulatory organization, or a state attorney general in a criminal proceeding.¹⁶ The Act defines monetary sanctions to include “any monies, including penalties, disgorgement, and interest, ordered to be paid” by the SEC.¹⁷ The bounty amount is determined at the discretion of the SEC subject to the ten- and thirty-percent outer limits. As guidance, the Act provides that the SEC “shall take into consideration” the significance of the information to the success of the enforcement action; the degree of assistance provided by the whistleblower; and the programmatic interest in deterring violations of the securities laws.¹⁸ While bounty determinations are subject to abuse-of-discretion review in an appropriate federal court of appeals, bounty amounts cannot be appealed.

Whistleblowers may submit information to the SEC anonymously. If they choose to do so, they must be represented by counsel, and the whistleblower’s identity must be disclosed before receiving a bounty.¹⁹ A company’s officers, directors, employees, shareholders, business competitors, employees of agents, consultants, distributors, vendors, contractors, service providers, or customers can all receive bounties under the Act. Certain individuals are prohibited from receiving award payments, including persons convicted of crimes related to the violation, those who learned of the disclosed information through the performance of an audit of financial statements as required by the securities laws, and certain federal regulatory and law enforcement employees.²⁰ The Act also excludes “any whistleblower who fails to submit information to the [SEC] in such form as the [SEC] may, by rule, require.”²¹ Finally, the Act bars rewards to persons who knowingly and willfully make false, fictitious, or fraudulent statements or representations, or who use any false writing or document knowing that it contains a false, fictitious, or fraudulent statement or entry.

¹⁴ *Id.* The Senate Banking Committee report explains that in “circumstances when bits and pieces of the whistleblower’s information were known to the media prior to the emergence of the whistleblower . . . [but] the critical components of the information [were] supplied by the whistleblower, the intent of the Committee is to require the SEC to reward such person(s) in accordance with the degree of assistance that was provided.” S. Rep. No. 111-176, at 111.

¹⁵ H.R. 4173, 111th Cong. § 922(a).

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ *Id.*

²⁰ *Id.*

²¹ *Id.*

2. The Dodd-Frank Act's Protection Provisions

In addition to the incentive provisions, Dodd-Frank significantly enhances whistleblower protections. Under the Act, employers are prohibited from discharging, demoting, suspending, threatening, harassing, or otherwise discriminating against whistleblowers who provide information to enforcement authorities.²² The Act creates a new private right of action for employees who experience retaliation as a result of “any lawful act done by the whistleblower [] (i) in providing information to the [SEC] in accordance with [the incentive provisions]; (ii) in initiating, testifying in, or assisting in any investigation or judicial or administrative action of the [SEC] based upon or related to such information; or (iii) in making disclosures that are required or protected” under the Sarbanes-Oxley Act, the Exchange Act, and “any other law, rule, or regulation subject to the jurisdiction of the [SEC].”²³

Under Dodd-Frank, for the first time, employees can bypass administrative remedies by bringing their claim in federal court from the outset.²⁴ The Act also provides greater remedies than previously available. In addition to reinstatement without loss of seniority and litigation costs (including expert witness fees and reasonable attorneys’ fees), employees can now recover double their lost wages with interest, instead of just lost wages.²⁵ Employees also have six years from the date of the violation to bring suit, or three years from the date when they knew or should reasonably have known of facts material to their right of action.²⁶ No action, however, may be brought more than ten years after the date of the violation.²⁷

Besides creating a private right of action, the Act contains provisions amending and strengthening the existing Sarbanes-Oxley anti-retaliation protections.²⁸ The Dodd-Frank provisions broaden the scope of coverage, extend the statute of limitations, exempt employee claims from arbitration, and clarify that claims removed to federal court can be tried before a jury. Dodd-Frank amends Section 806 of Sarbanes-Oxley to broaden the scope of coverage by clarifying that Section 806’s whistleblower provisions apply to employees of subsidiaries of publicly traded parent companies “whose financial information is included in the consolidated financial statements of [parent companies].”²⁹

²² *Id.*

²³ *Id.* Dodd-Frank also creates a private right of action for employees in the financial services industry who experience retaliation in connection with their disclosure of information regarding fraudulent or unlawful conduct related to the offering or provision of a consumer financial product or service. H.R. 4173, 111th Cong. § 1057.

²⁴ H.R. 4173, 111th Cong. § 922(a).

²⁵ *Id.*

²⁶ *Id.*

²⁷ *Id.*

²⁸ In addition to amending the Sarbanes-Oxley Act, Dodd-Frank amends the Commodity Exchange Act, 7 U.S.C. § 1 et seq., to create an incentive program and whistleblower provisions similar to those now provided by Section 21F of the Exchange Act, including a new private right of action. H.R. 4173, 111th Cong. § 748. Dodd-Frank also amends the anti-retaliation provisions of the False Claims Act, 31 U.S.C. § 3730(h), by expanding coverage of protected conduct to include associational discrimination and by clarifying the statute of limitations for actions brought under the False Claims Act. H.R. 4173, 111th Cong. § 1079A.

²⁹ H.R. 4173, 111th Cong. § 929A.

This amendment closes a loophole that, in the past, permitted parent companies that employed most of their workforce through non-publicly traded subsidiaries to avoid Sarbanes-Oxley liability. In addition to employees of subsidiaries, Dodd-Frank further expands the reach of Sarbanes-Oxley to include protection for employees of nationally-recognized statistical ratings organizations.³⁰

Instead of a ninety-day statute of limitations, employees now have 180 days to initiate a Sarbanes-Oxley action and also may elect to try their cases in federal court before a jury.³¹ Finally, Dodd-Frank reverses judicial precedent and amends Section 806 of Sarbanes-Oxley by declaring void any “agreement, policy form, or condition of employment, including by a predispute arbitration agreement” that waives an employee’s rights and remedies against retaliation in connection with a whistleblowing event.³²

B. The SEC’s Policy Regarding Cooperation By Individuals

The Dodd-Frank whistleblower incentive and protection provisions complement the SEC’s release earlier this year of a policy statement describing the analytical framework it uses to evaluate cooperation by individuals. When Robert Khuzami, the SEC’s Director of the Division of Enforcement, introduced the policy, he described it as “a potential game-changer for the Division of Enforcement.”³³ The policy — part of a larger initiative intended to encourage individual and company cooperation — is designed to incentivize early and extensive cooperation with SEC investigations and enforcement actions by allowing diminished sanctions for individuals providing information regarding violations of the securities laws. The initiative also authorizes new cooperation tools, including cooperation agreements, deferred prosecution agreements, non-prosecution agreements, expedited immunity requests, and proffer agreements and oral assurances.³⁴

The policy statement describes four general considerations the SEC analyzes when evaluating an individual’s cooperation. These include: (1) the level of assistance provided by the individual; (2) the importance of the underlying investigation or enforcement matter; (3) the societal interest in ensuring the individual is held accountable for his or her misconduct; and (4) the appropriateness of cooperation credit based on future risk of wrongdoing. The policy statement details numerous specific factors that inform each of the four considerations.

First, in analyzing the assistance provided by the cooperating individual, the SEC will consider the “value” and “nature” of the individual’s cooperation. Among other factors, the SEC will weigh the extent, quality, and timeliness of the individual’s cooperation. The SEC will also consider whether cooperation is voluntary, the types of

³⁰ H.R. 4173, 111th Cong. § 922(b).

³¹ H.R. 3763, 107th Cong. § 806 (2002); H.R. 4173, 111th Cong. § 922(c).

³² H.R. 4173, 111th Cong. § 922(c).

³³ SEC, SEC Announces Initiative to Encourage Individuals and Companies to Cooperate and Assist in Investigations (Jan. 13, 2010).

³⁴ The initiative is contained in the SEC’s Enforcement Manual in a chapter entitled “Fostering Cooperation.” An excerpt from the Manual is attached at Appendix H.

assistance provided by the individual, whether the individual encouraged or authorized others to cooperate, and whether the individual disclosed information not otherwise obtainable.

Second, in analyzing the importance of the underlying matter, the SEC will consider the “character of the investigation” and the dangers presented by the underlying violations to investors and others. The character of the investigation is assessed by considering whether the subject matter is an enforcement priority, the type of securities violation, the age and duration of misconduct, and the number and frequency of violations. In analyzing the dangers presented by the underlying violations, the SEC will consider the amount of harm or potential harm caused by the misconduct, the type of harm, and the number of individuals or entities harmed.

Third, in analyzing the “societal interest in holding the cooperating individual fully accountable” for misconduct, the SEC will consider, among other factors, the severity of the misconduct, the culpability or intent of the individual, the degree to which the individual tolerated illegal activity, the individual’s efforts to remedy any harm caused, and the sanctions imposed by other authorities.

Finally, in analyzing the appropriateness of cooperation credit, the SEC will examine the “[p]rofile of the individual.” Enforcement officials will consider, among other factors, the individual’s history of lawfulness, acceptance of responsibility, and whether the individual will have an opportunity to commit future violations of the securities laws based on his or her occupation or position within a company.

While the initiative also reiterates the SEC’s policy on cooperation by companies contained in the Seaboard Report and makes available to companies the same tools available to individuals, it reflects — along with the Dodd-Frank provisions — a new emphasis and reliance by the SEC on individuals in meeting its enforcement objectives.

III. A New Dynamic and the Changing Role of the SEC

Over the past two years, SEC reforms have focused on restoring confidence through the more aggressive pursuit of violators and new enforcement structures and tactics. To that end, the SEC has implemented extensive policy and procedural changes intended to give enforcement authorities greater discretion in initiating and conducting investigations, bringing enforcement actions, and imposing penalties. This has created a new enforcement dynamic that is more prosecutorial, faster, and more complex for companies to navigate.

Many of the changes permit the SEC to operate more like a criminal prosecutor. The new cooperation initiative, for example, authorizes the use of deferred prosecution agreements and non-prosecution agreements in exchange for cooperation, which are tools routinely used as part of corporate crime investigations by the DOJ. In a speech before the Society of American Business Editors and Writers, Khuzami noted that “cooperator testimony is the lifeblood of criminal prosecutions . . . [and] cooperating witnesses can be the master key that unlocks the intricacies of cases involving complex transactions that

might otherwise escape detection, or enable authorities to apprehend the higher-ups whose culpability can be the most challenging to establish.”³⁵

There are also initiatives to speed up investigations and make them more efficient. Senior officers at each regional SEC office now have delegated authority to issue formal orders of investigation, which allows the enforcement staff to serve subpoenas. Before 2009, all formal orders were required to be issued by the SEC itself. The change allows the SEC to obtain evidence faster, freeze assets earlier, and better coordinate enforcement efforts. In addition, the SEC has streamlined the process for submitting witness immunity requests to the DOJ for cooperating individuals. Specialized units have also been created in specific enforcement areas.

While these changes themselves have already resulted in increased enforcement, companies now have to navigate even more complex investigations. This is especially the case now that individuals can trade information for (1) the promise of a large bounty; (2) powerful protections against employer retaliation; and (3) reduced exposure and cooperation credit.

IV. How Companies Can Respond

The new whistleblower provisions and the encouragement of individual cooperation bring with them the likelihood of increased enforcement actions against companies based on alleged violations of the securities laws. In light of this new environment, companies should consider changes in each of the following areas:

A. Compliance and Ethics Programs

The whistleblower provisions and the potential to collect a substantial cash bounty incentivize employees to ignore corporate compliance systems and ethics programs. In light of Dodd-Frank’s whistleblower incentive provisions, companies should review their compliance and ethics programs. This should be done with an eye toward ensuring that the programs allow companies to identify, investigate, and handle potential misconduct quickly and effectively.

Competing directly with the whistleblower provisions and finding ways to learn information first and incentivize employees to report up (instead of out) will be challenging. To encourage employees to voice concerns internally, companies should cultivate a compliance culture that emphasizes, values, and rewards ethical behavior, integrity, and accountability. Companies should make clear that adherence to the securities laws is a consistent and core value and that concerns raised internally will be taken seriously. Often, whistleblowers go outside the company only after they conclude that the company has not listened to them.

Although the specific circumstances of companies differ, general areas companies can consider when evaluating their compliance and ethics programs include:

³⁵ Robert Khuzami, SEC Director of the Division of Enforcement, Speech to the Society of American Business Editors and Writers (Mar. 19, 2010).

- Ensuring that company personnel are regularly educated and trained on the requirements of securities laws and how to comply with them to prevent uninformed individuals from making false or misguided reports;
- Ensuring that management is trained to recognize whistleblower complaints, report complaints, and respond to complaints;
- Ensuring that programs are reviewed and updated periodically to account for changes in the law and the company's business;
- Ensuring appropriate disciplinary procedures are in place that address conduct that violates the securities laws and the failure to take reasonable steps to prevent and detect misconduct by others;
- Verifying that compliance audits and risk assessments are regularly performed to detect potential risks or offenses before they turn into violations and before discovery outside the company is likely;
- Verifying that internal reporting mechanisms such as anonymous hotlines are clearly established and ensuring that reported information and tips are quickly and appropriately escalated;
- Assessing which subsidiaries or affiliates are now covered by Sarbanes-Oxley and strengthening internal reporting procedures to encourage employees to raise concerns internally;
- Ensuring that employee conduct manuals expressly require employees to report potential misconduct, and that employees are regularly trained on and acknowledge this obligation; and
- Ensuring that third-party contracts include an obligation that the third party provides notice of potential compliance issues.

In reviewing their compliance and ethics programs, companies can also consider the pending amendments to the U.S. Sentencing Guidelines (the "Guidelines") scheduled to take effect in November 2010 (absent congressional action otherwise), which provide a reduction in culpability score for companies that have in place an "effective" compliance and ethics program at the time of a violation.³⁶ Enforcement authorities use the Guidelines as a starting point when calculating fines and settlement figures. Under the amendments, sentencing credit is available to companies that meet the criteria for having "effective compliance and ethics programs," which include:

- Direct reporting obligations. The persons with operational responsibility for the corporation's compliance and ethics program must have "direct

³⁶ U.S. Sent'g Comm'n, Amendments to the Sentencing Guidelines §§ 8B2.1, 8C2.5 (May 3, 2010). An excerpt from the amendments to the Guidelines is attached at Appendix I.

reporting obligations” to the governing authority including, for example, the board of directors or the audit committee. A reporting obligation to the general counsel or another high-level officer would not meet this requirement.

- Discovery of offense. The compliance and ethics program must detect the offense before discovery outside the corporation is reasonably likely.
- Reporting of offense. The organization must promptly report the offense to the appropriate federal authorities.
- Involvement of compliance personnel. No person with operational responsibility for the compliance and ethics program participated in, condoned, or was willfully ignorant of the offense.³⁷

The commentary to the amendments provides additional guidance regarding how a company can establish an effective compliance and ethics program. “Direct reporting authority,” for example, is the autonomy and authority granted to the person in charge of the compliance program to “communicate personally” with the board or its audit committee where there is suspected criminal conduct. In addition, the person in charge of the compliance program must report to the board at least annually regarding the implementation and effectiveness of the compliance program. Companies should thus ensure that their written policies provide for direct reporting to the board to maximize their chances of qualifying for the sentencing credit based on a finding that their compliance and ethics program is “effective.”

Finally, companies can participate in the comment process associated with SEC rule-making to communicate their concerns regarding the potential of the Dodd-Frank whistleblower provisions to undermine corporate compliance programs. Companies should emphasize that the goal of such programs is to detect misconduct early on and promptly implement remedial measures. For compliance and ethics programs to remain effective, the regulations could provide that whistleblowers should at least attempt to exhaust internal remedies before reporting to the government.

B. Anti-Retaliation Policies

In addition to finding ways to minimize violations and events that create whistleblowing opportunities, companies need to take steps to minimize the risk of whistleblower retaliation claims. While the whistleblower incentive provisions will likely cause an increase in the number of whistleblower claims, the protection provisions will also likely cause an increase in the costs and risks associated with defending potential retaliation claims. In light of the enhanced protections and remedies provided to whistleblowers in Dodd-Frank, companies should review the effectiveness of personnel and anti-retaliation policies.

³⁷ See *id.* at § 8C2.5.

Anti-retaliation policies should ensure that measures are in place to prevent actual or perceived mistreatment of known whistleblowers. Disciplinary and evaluation procedures should require that the reasons for taking specific employment actions are clearly and adequately documented. In evaluating anti-retaliation policies, companies must be careful not to discourage employees from turning to enforcement authorities, as such action could be used by employees as evidence of retaliatory intent. In addition, companies should revise their document-retention policies to retain personnel files and other records that could be used to defend against a potential retaliation claim for at least ten years, the maximum statute of limitations period under the newly-created private right of action.

Under the amendments to Sarbanes-Oxley, companies can no longer avoid litigation of retaliation claims through pre-dispute arbitration agreements or general release and settlement agreements. In addition, anti-retaliation policies will need to be updated and modified to include subsidiaries and affiliates that are now subject to potential whistleblower exposure.

C. Responding to Potential Misconduct

In light of the new whistleblower provisions and emphasis on individual cooperation, as well as the faster and more streamlined processes at the SEC, companies will need to respond to potential misconduct much more frequently and quickly. No company will want to “lose the race” to get on top of the facts. For that reason, companies should consider having procedures (and counsel) in place and ready to respond promptly to discoveries of potential misconduct that could create liability. A fast and effective response will boost a company’s credibility and possibly translate into more lenient treatment if enforcement authorities eventually become involved.

D. Self-Reporting Violations, Cooperating With Enforcement Authorities, and Public Disclosure

In the past, companies faced a delicate and complex assessment when deciding whether and when to self-report potential misconduct to enforcement authorities. On one hand, making a voluntary disclosure increases the possibility of mitigating civil and criminal penalties, or avoiding prosecution altogether. The Seaboard Report, for example, states that the SEC will consider a number of factors, including voluntary disclosure and cooperation, when determining whether to initiate an enforcement action or civil proceedings against a company for violations of the securities laws. Other benefits of self-reporting include the ability to define the misconduct and put in place remedial measures.

On the other hand, self-reporting contains significant risks. It could bring undue enforcement attention to a minor matter that would otherwise go unnoticed. It could also prompt the filing of shareholder lawsuits.

The new incentives change this balance. Now, it is more likely that individuals — who may not even be company employees — will take action that triggers a

government investigation. Companies will likely self-report earlier and more often to maximize the chance of receiving cooperation credit.

E. Ancillary Effects

The potential for more investigations, enforcement actions, and retaliation claims will have additional effects. First, in dealing with increased legal exposure, companies will need to be prepared to address public and investor relations issues that these actions and related disclosures will cause.

Second, plaintiffs' lawyers may draw on the fact of an SEC investigation, or a whistleblower claim, to bring derivative or securities class action lawsuits. In doing so, plaintiffs' lawyers may attempt to use the Freedom of Information Act to obtain documents related to SEC investigations, or information disclosed in whistleblower lawsuits as a means to bolster their complaints.

F. Insurance

The likely increase in enforcement actions, investigations, and private securities litigation also raises questions about the adequacy of companies' insurance coverage. In light of the new whistleblower provisions and emphasis on individual cooperation, companies should consider:

- Whether covered "claims" include internal investigations;
- Whether covered "claims" include civil, criminal, administrative, and regulatory investigations, both informal and formal; and
- Whether existing policy limits are adequate.

Federal Prosecution of Business Organizations

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U.S. Department of Justice

Office of the Deputy Attorney General

The Deputy Attorney General

Washington, D.C. 20530

January 20, 2003

MEMORANDUM

TO: Heads of Department Components
United States Attorneys

FROM: Larry D. Thompson
Deputy Attorney General

SUBJECT: Principles of Federal Prosecution of Business Organizations

As the Corporate Fraud Task Force has advanced in its mission, we have confronted certain issues in the principles for the federal prosecution of business organizations that require revision in order to enhance our efforts against corporate fraud. While it will be a minority of cases in which a corporation or partnership is itself subjected to criminal charges, prosecutors and investigators in every matter involving business crimes must assess the merits of seeking the conviction of the business entity itself.

Attached to this memorandum are a revised set of principles to guide Department prosecutors as they make the decision whether to seek charges against a business organization. These revisions draw heavily on the combined efforts of the Corporate Fraud Task Force and the Attorney General's Advisory Committee to put the results of more than three years of experience with the principles into practice.

The main focus of the revisions is increased emphasis on and scrutiny of the authenticity of a corporation's cooperation. Too often business organizations, while purporting to cooperate with a Department investigation, in fact take steps to impede the quick and effective exposure of the complete scope of wrongdoing under investigation. The revisions make clear that such conduct should weigh in favor of a corporate prosecution. The revisions also address the efficacy of the corporate governance mechanisms in place within a corporation, to ensure that these measures are truly effective rather than mere paper programs.

Further experience with these principles may lead to additional adjustments. I look forward to hearing comments about their operation in practice. Please forward any comments to Christopher Wray, the Principal Associate Deputy Attorney General, or to Andrew Hruska, my Senior Counsel.

Federal Prosecution of Business Organizations¹

I. Charging a Corporation: General

A. General Principle: Corporations should not be treated leniently because of their artificial nature nor should they be subject to harsher treatment. Vigorous enforcement of the criminal laws against corporate wrongdoers, where appropriate results in great benefits for law enforcement and the public, particularly in the area of white collar crime. Indicting corporations for wrongdoing enables the government to address and be a force for positive change of corporate culture, alter corporate behavior, and prevent, discover, and punish white collar crime.

B. Comment: In all cases involving corporate wrongdoing, prosecutors should consider the factors discussed herein. First and foremost, prosecutors should be aware of the important public benefits that may flow from indicting a corporation in appropriate cases. For instance, corporations are likely to take immediate remedial steps when one is indicted for criminal conduct that is pervasive throughout a particular industry, and thus an indictment

often provides a unique opportunity for deterrence on a massive scale. In addition, a corporate indictment may result in specific deterrence by changing the culture of the indicted corporation and the behavior of its employees. Finally, certain crimes that carry with them a substantial risk of great public harm, e.g., environmental crimes or financial frauds, are by their nature most likely to be committed by businesses, and there may, therefore, be a substantial federal interest in indicting the corporation.

Charging a corporation, however, does not mean 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, even in the face of offers of corporate guilty pleas.

Corporations are "legal persons," capable of suing and being sued, and capable of committing crimes. Under the doctrine of *respondereat superior*, a corporation may be held criminally liable for the illegal acts of its directors, officers, employees, and agents. To hold a corporation liable for these actions, the government must establish that the corporate agent's actions (i) were within the scope of his duties and (ii) were intended, at least in part, to benefit the corporation. In all cases involving wrongdoing by corporate agents, prosecutors should consider the corporation, as well as the responsible individuals, as potential criminal targets.

Agents, however, may act for mixed reasons -- both for self-aggrandizement (both direct and indirect) and for the benefit of the corporation, and a corporation may be held liable as long as one motivation of its agent is to benefit the corporation. In *United States v. Automated Medical Laboratories*, 770 F.2d 399 (4th Cir. 1985), the court affirmed the corporation's conviction for the actions of a subsidiary's employee despite its claim that the employee was acting for his own benefit, namely his "ambitious nature and his desire to ascend the corporate ladder." The court stated, "*Partucci* was clearly acting in part to benefit AML since his advancement within the corporation depended on AML's well-being and its lack of difficulties with the FDA." Similarly, in *United States v. Cincotta*, 689 F.2d 238, 241-42 (1st Cir. 1982), the court held, "criminal liability may be imposed on the corporation only where the agent is acting within the scope of his employment. That, in turn, requires that the agent be performing acts of the kind which he is authorized to perform, and those acts must be motivated -- at least in part -- by an intent to benefit the corporation." Applying this test, the court upheld the corporation's conviction, notwithstanding the substantial personal benefit reaped by its miscreant agents, because the fraudulent scheme required money to pass through the corporation's treasury and the fraudulently obtained goods were resold to the corporation's customers in the corporation's name. As the court concluded, "Mystic--not the individual defendants--was making money by selling oil that it had not paid for."

Moreover, the corporation need not even necessarily profit from its agent's actions for it to be held liable. In *Automated Medical Laboratories*, the Fourth Circuit stated:

[B]enefit is not a "touchstone of criminal corporate liability; benefit at best is an evidential, not an operative, fact." Thus, whether the agent's actions ultimately redounded to the benefit of the corporation is less significant than whether the agent acted with the intent to benefit the corporation. The basic purpose of requiring that an agent have acted with the intent to benefit the corporation, however, is to insulate the corporation from criminal liability for actions of its agents which be inimical to the interests of the corporation or which may have been undertaken solely to advance the interests of that agent or of a party other than the corporation.

770 F.2d at 407 (emphasis added; quoting *Old Monastery Co. v. United States*, 147 F.2d 905, 908 (4th Cir.), cert. denied, 326 U.S. 734 (1945)).

II. Charging a Corporation: Factors to Be Considered

A. General Principle: Generally, prosecutors should apply the same factors in determining whether to charge a corporation as they do with respect to individuals. See USAM § 9-27.220, *et seq.* Thus, the prosecutor should weigh all of the factors normally considered in the sound exercise of prosecutorial judgment: the sufficiency of the evidence; the likelihood of success at trial; the probable deterrent, rehabilitative, and other consequences of conviction; and the adequacy of noncriminal approaches. See *id.* However, due to the nature of the corporate "person," some additional factors are present. In conducting an investigation, determining whether to bring

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charges, and negotiating plea agreements, prosecutors should consider the following factors in reaching a decision as to the proper treatment of a corporate target:

1. the nature and seriousness of the offense, including the risk of harm to the public, and applicable policies and priorities, if any, governing the prosecution of corporations for particular categories of crime (see section III, *infra*);
2. the pervasiveness of wrongdoing within the corporation, including the complicity in, or condonation of, the wrongdoing by corporate management (see section IV, *infra*);
3. the corporation's history of similar conduct, including prior criminal, civil, and regulatory enforcement actions against it (see section V, *infra*);
4. the corporation's timely and voluntary disclosure of wrongdoing and its willingness to cooperate in the investigation of its agents, including, if necessary, the waiver of corporate attorney-client and work product protection (see section VI, *infra*);
5. the existence and adequacy of the corporation's compliance program (see section VII, *infra*);
6. the corporation's remedial actions, including any efforts to implement an effective corporate compliance program or to improve an existing one, to replace responsible management, to discipline or terminate wrongdoers, to pay restitution, and to cooperate with the relevant government agencies (see section VIII, *infra*);
7. collateral consequences, including disproportionate harm to shareholders, pension holders and employees not proven personally culpable and impact on the public arising from the prosecution (see section IX, *infra*); and
8. the adequacy of the prosecution of individuals responsible for the corporation's malfeasance;
9. the adequacy of remedies such as civil or regulatory enforcement actions (see section X, *infra*).

B. Comment: As with the factors relevant to charging natural persons, the foregoing factors are intended to provide guidance rather than to mandate a particular result. The factors listed in this section are intended to be illustrative of those that should be considered and not a complete or exhaustive list. Some or all of these factors may or may not apply to specific cases, and in some cases one factor may override all others. The nature and seriousness of the offense may be such as to warrant prosecution regardless of the other factors. Further, national law enforcement policies in various enforcement areas may require that more or less weight be given to certain of these factors than to others.

In making a decision to charge a corporation, the prosecutor generally has wide latitude in determining when, whom, how, and even whether to prosecute for violations of Federal criminal law. In exercising that discretion, prosecutors should consider the following general statements of principles that summarize appropriate considerations to be weighed and desirable practices to be followed in discharging their prosecutorial responsibilities. In doing so, prosecutors should ensure that the general purposes of the criminal law -- assurance of warranted punishment, deterrence of further criminal conduct, protection of the public from dangerous and fraudulent conduct, rehabilitation of offenders, and restitution for victims and affected communities -- are adequately met, taking into account the special nature of the corporate "person."

III. Charging a Corporation: Special Policy Concerns

A. General Principle: The nature and seriousness of the crime, including the risk of harm to the public from the criminal conduct, are obviously primary factors in determining whether to charge a corporation. In addition, corporate conduct, particularly that of national and multi-national corporations, necessarily intersects with federal economic, taxation, and criminal law enforcement policies. In applying these principles, prosecutors must consider the practices and policies of the appropriate Division of the Department, and must comply with those policies to the extent required.

B. Comment: In determining whether to charge a corporation, prosecutors should take into account federal law enforcement priorities as discussed above. See USAM § 9-27-230. In addition, however, prosecutors must be aware of the specific policy goals and incentive programs established by the respective Divisions and regulatory agencies. Thus, whereas natural persons may be given incremental degrees of credit (ranging from immunity to lesser charges to sentencing considerations) for turning themselves in, making statements against their penal interest, and cooperating in the government's investigation of their own and others' wrongdoing, the same approach may not be appropriate in all circumstances with respect to corporations. As an example, it is entirely proper in many investigations for a prosecutor to consider the corporation's pre-indictment conduct, e.g., voluntary disclosure, cooperation, remediation or restitution, in determining whether to seek an indictment. However, this would not necessarily be appropriate in an antitrust investigation, in which antitrust violations, by definition, go to the heart of the corporation's business and for which the Antitrust Division has therefore established a firm policy, understood in the business community, that credit should not be given at the charging stage for a compliance program and that amnesty is available only to the first corporation to make full disclosure to the government. As another example, the Tax Division has a strong preference for prosecuting responsible individuals, rather than entities, for corporate tax offenses. Thus, in determining whether or not to charge a corporation, prosecutors should consult with the Criminal, Antitrust, Tax, and Environmental and Natural Resources Divisions, if appropriate or required.

IV. Charging a Corporation: Pervasiveness of Wrongdoing Within the Corporation

A. General Principle: A corporation can only act through natural persons, and it is therefore held responsible for the acts of such persons fairly attributable to it. Charging a corporation for even minor misconduct may be appropriate where the wrongdoing was pervasive and was undertaken by a large number of employees or by all the employees in a particular role within the corporation, e.g., salesmen or procurement officers, or was condoned by upper management. On the other hand, in certain limited circumstances, it may not be appropriate to impose liability upon a corporation, particularly one with a compliance program in place, under a strict *respondeat superior* theory for the single isolated act of a rogue employee. There is, of course, a wide spectrum between these two extremes, and a prosecutor should exercise sound discretion in evaluating the pervasiveness of wrongdoing within a corporation.

B. Comment: Of these factors, the most important is the role of management. Although acts of even low-level employees may result in criminal liability, a corporation is directed by its management and management is responsible for a corporate culture in which criminal conduct is either discouraged or tacitly encouraged. As stated in commentary to the Sentencing Guidelines:

Pervasiveness [is] case specific and [will] depend on the number, and degree of responsibility, of individuals [with] substantial authority ... who participated in, condoned, or were willfully ignorant of the offense. Fewer individuals need to be involved for a finding of pervasiveness if those individuals exercised a relatively high degree of authority. Pervasiveness can occur either within an organization as a whole or within a unit of an organization.

USSG §8C2.5, comment. (n. 4).

V. Charging a Corporation: The Corporation's Past History

A. General Principle: Prosecutors may consider a corporation's history of similar conduct, including prior criminal, civil, and regulatory enforcement actions against it, in determining whether to bring criminal charges.

B. Comment: A corporation, like a natural person, is expected to learn from its mistakes. A history of similar conduct may be probative of a corporate culture that encouraged, or at least condoned, such conduct, regardless of any compliance programs. Criminal prosecution of a corporation may be particularly appropriate where the corporation previously had been subject to non-criminal guidance, warnings, or sanctions, or previous criminal charges, and yet it either had not taken adequate action to prevent future unlawful conduct or had continued to engage in the conduct in spite of the warnings or enforcement actions taken against it. In making this determination, the corporate structure itself, e.g., subsidiaries or operating divisions, should be ignored, and enforcement actions taken against the corporation or any of its divisions, subsidiaries, and affiliates should be considered. See USSG § 8C2.5(c) & comment. (n. 6).

VI. Charging a Corporation: Cooperation and Voluntary Disclosure

A. General Principle: In determining whether to charge a corporation, that corporation's timely and voluntary disclosure of wrongdoing and its willingness to cooperate with the government's investigation may be relevant factors. In gauging the extent of the corporation's cooperation, the prosecutor may consider the corporation's willingness to identify the culprits within the corporation, including senior executives; to make witnesses available; to disclose the complete results of its internal investigation; and to waive attorney-client and work product protection.

B. Comment: In investigating wrongdoing by or within a corporation, a prosecutor is likely to encounter several obstacles resulting from the nature of the corporation itself. It will often be difficult to determine which individual took which action on behalf of the corporation. Lines of authority and responsibility may be shared among operating divisions or departments, and records and personnel may be spread throughout the United States or even among several countries. Where the criminal conduct continued over an extended period of time, the culpable or knowledgeable personnel may have been promoted, transferred, or fired, or they may have quit or retired. Accordingly, a corporation's cooperation may be critical in identifying the culprits and locating relevant evidence.

In some circumstances, therefore, granting a corporation immunity or amnesty or pretrial diversion may be considered in the course of the government's investigation. In such circumstances, prosecutors should refer to the principles governing non-prosecution agreements generally. See USAM § 9-27.600-650. These principles permit a non prosecution agreement in exchange for cooperation when a corporation's "timely cooperation appears to be necessary to the public interest and other means of obtaining the desired cooperation are unavailable or would not be effective." Prosecutors should note that in the case of national or multi-national corporations, multi-district or global agreements may be necessary. Such agreements may only be entered into with the approval of each affected district or the appropriate Department official. See USAM §9-27.641.

In addition, the Department, in conjunction with regulatory agencies and other executive branch departments, encourages corporations, as part of their compliance programs, to conduct internal investigations and to disclose their findings to the appropriate authorities. Some agencies, such as the SEC and the EPA, as well as the Department's Environmental and Natural Resources Division, have formal voluntary disclosure programs in which self-reporting, coupled with remediation and additional criteria, may qualify the corporation for amnesty or reduced sanctions.² Even in the absence of a formal program, prosecutors may consider a corporation's timely and voluntary disclosure in evaluating the adequacy of the corporation's compliance program and its management's commitment to the compliance program. However, prosecution and economic policies specific to the industry or statute may require prosecution notwithstanding a corporation's willingness to cooperate. For example, the Antitrust Division offers amnesty only to the first corporation to agree to cooperate. This creates a strong incentive for corporations participating in anti-competitive conduct to be the first to cooperate. In addition, amnesty, immunity, or reduced sanctions may not be appropriate where the corporation's business is permeated with fraud or other crimes.

One factor the prosecutor may weigh in assessing the adequacy of a corporation's cooperation is the completeness of its disclosure including, if necessary, a waiver of the attorney-client and work product protections, both with respect to its internal investigation and with respect to communications between specific officers, directors and employees and counsel. Such waivers permit the government to obtain statements of possible witnesses, subjects, and targets, without having to negotiate individual cooperation or immunity agreements. In addition, they are often critical in enabling the government to evaluate the completeness of a corporation's voluntary disclosure and cooperation. Prosecutors may, therefore, request a waiver in appropriate circumstances.³ The Department does not, however, consider waiver of a corporation's attorney-client and work product protection an absolute requirement, and prosecutors should consider the willingness of a corporation to waive such protection when necessary to provide timely and complete information as one factor in evaluating the corporation's cooperation.

Another factor to be weighed by the prosecutor is whether the corporation appears to be protecting its culpable employees and agents. Thus, while cases will differ depending on the circumstances, a corporation's promise of support to culpable employees and agents, either through the advancing of attorneys fees,⁴ through retaining the employees without sanction for their misconduct, or through providing information to the employees about the government's investigation pursuant to a joint defense agreement, may be considered by the prosecutor in weighing the extent and value of a corporation's cooperation. By the same token, the prosecutor should be

wary of attempts to shield corporate officers and employees from liability by a willingness of the corporation to plead guilty.

Another factor to be weighed by the prosecutor is whether the corporation, while purporting to cooperate, has engaged in conduct that impedes the investigation (whether or not rising to the level of criminal obstruction). Examples of such conduct include: overly broad assertions of corporate representation of employees or former employees; inappropriate directions to employees or their counsel, such as directions not to cooperate openly and fully with the investigation including, for example, the direction to decline to be interviewed; making presentations or submissions that contain misleading assertions or omissions; incomplete or delayed production of records; and failure to promptly disclose illegal conduct known to the corporation.

Finally, a corporation's offer of cooperation does not automatically entitle it to immunity from prosecution. A corporation should not be able to escape liability merely by offering up its directors, officers, employees, or agents as in lieu of its own prosecution. Thus, a corporation's willingness to cooperate is merely one relevant factor, that needs to be considered in conjunction with the other factors, particularly those relating to the corporation's past history and the role of management in the wrongdoing.

VII. Charging a Corporation: Corporate Compliance Programs

A. General Principle: Compliance programs are established by corporate management to prevent and to detect misconduct and to ensure that corporate activities are conducted in accordance with all applicable criminal and civil laws, regulations, and rules. The Department encourages such corporate self-policing, including voluntary disclosures to the government of any problems that a corporation discovers on its own. However, the existence of a compliance program is not sufficient, in and of itself, to justify not charging a corporation for criminal conduct undertaken by its officers, directors, employees, or agents. Indeed, the commission of such crimes in the face of a compliance program may suggest that the corporate management is not adequately enforcing its program. In addition, the nature of some crimes, e.g., antitrust violations, may be such that national law enforcement policies mandate prosecutions of corporations notwithstanding the existence of a compliance program.

B. Comment: A corporate compliance program, even one specifically prohibiting the very conduct in question, does not absolve the corporation from criminal liability under the doctrine of *respondeat superior*. See *United States v. Basic Construction Co.*, 711 F.2d 570 (4th Cir. 1983) ("a corporation may be held criminally responsible for antitrust violations committed by its employees if they were acting within the scope of their authority, or apparent authority, and for the benefit of the corporation, even if... such acts were against corporate policy or express instructions."). In *United States v. Hilton Hotels Corp.*, 467 F.2d 1000 (9th Cir. 1972), *cert. denied*, 409 U.S. 1125 (1973), the Ninth Circuit affirmed antitrust liability based upon a purchasing agent for a single hotel threatening a single supplier with a boycott unless it paid dues to a local marketing association, even though the agent's actions were contrary to corporate policy and directly against express instructions from his superiors. The court reasoned that Congress, in enacting the Sherman Antitrust Act, "intended to impose liability upon business entities for the acts of those to whom they choose to delegate the conduct of their affairs, thus stimulating a maximum effort by owners and managers to assure adherence by such agents to the requirements of the Act."⁵ It concluded that "general policy statements" and even direct instructions from the agent's superiors were not sufficient; "Appellant could not gain exculpation by issuing general instructions without undertaking to enforce those instructions by means commensurate with the obvious risks." See also *United States v. Beusch*, 596 F.2d 871, 878 (9th Cir. 1979) ("[A] corporation may be liable for the acts of its employees done contrary to express instructions and policies, but ... the existence of such instructions and policies may be considered in determining whether the employee in fact acted to benefit the corporation."); *United States v. American Radiator & Standard Sanitary Corp.*, 433 F.2d 174 (3rd Cir. 1970) (affirming conviction of corporation based upon its officer's participation in price-fixing scheme, despite corporation's defense that officer's conduct violated its "rigid anti-fraternization policy" against any socialization (and exchange of price information) with its competitors; "When the act of the agent is within the scope of his employment or his apparent authority, the corporation is held legally responsible for it, although what he did may be contrary to his actual instructions and may be unlawful.").

While the Department recognizes that no compliance program can ever prevent all criminal activity by a corporation's employees, the critical factors in evaluating any program are whether the program is adequately designed for maximum effectiveness in preventing and detecting wrongdoing by employees and whether corporate management is enforcing the program or is tacitly encouraging or pressuring employees to engage in misconduct to achieve business objectives. The Department has no formal guidelines for corporate compliance

programs. The fundamental questions any prosecutor should ask are: "Is the corporation's compliance program well designed?" and "Does the corporation's compliance program work?" In answering these questions, the prosecutor should consider the comprehensiveness of the compliance program; the extent and pervasiveness of the criminal conduct; the number and level of the corporate employees involved; the seriousness, duration, and frequency of the misconduct; and any remedial actions taken by the corporation, including restitution, disciplinary action, and revisions to corporate compliance programs.⁶ Prosecutors should also consider the promptness of any disclosure of wrongdoing to the government and the corporation's cooperation in the government's investigation. In evaluating compliance programs, prosecutors may consider whether the corporation has established corporate governance mechanisms that can effectively detect and prevent misconduct. For example, do the corporation's directors exercise independent review over proposed corporate actions rather than unquestioningly ratifying officers' recommendations; are the directors provided with information sufficient to enable the exercise of independent judgment, are internal audit functions conducted at a level sufficient to ensure their independence and accuracy and have the directors established an information and reporting system in the organization reasonable designed to provide management and the board of directors with timely and accurate information sufficient to allow them to reach an informed decision regarding the organization's compliance with the law. *In re: Caremark*, 698 A.2d 959 (Del. Ct. Chan. 1996).

Prosecutors should therefore attempt to determine whether a corporation's compliance program is merely a "paper program" or whether it was designed and implemented in an effective manner. In addition, prosecutors should determine whether the corporation has provided for a staff sufficient to audit, document, analyze, and utilize the results of the corporation's compliance efforts. In addition, prosecutors should determine whether the corporation's employees are adequately informed about the compliance program and are convinced of the corporation's commitment to it. This will enable the prosecutor to make an informed decision as to whether the corporation has adopted and implemented a truly effective compliance program that, when consistent with other federal law enforcement policies, may result in a decision to charge only the corporation's employees and agents.

Compliance programs should be designed to detect the particular types of misconduct most likely to occur in a particular corporation's line of business. Many corporations operate in complex regulatory environments outside the normal experience of criminal prosecutors. Accordingly, prosecutors should consult with relevant federal and state agencies with the expertise to evaluate the adequacy of a program's design and implementation. For instance, state and federal banking, insurance, and medical boards, the Department of Defense, the Department of Health and Human Services, the Environmental Protection Agency, and the Securities and Exchange Commission have considerable experience with compliance programs and can be very helpful to a prosecutor in evaluating such programs. In addition, the Fraud Section of the Criminal Division, the Commercial Litigation Branch of the Civil Division, and the Environmental Crimes Section of the Environment and Natural Resources Division can assist U.S. Attorneys' Offices in finding the appropriate agency office and in providing copies of compliance programs that were developed in previous cases.

VIII. Charging a Corporation: Restitution and Remediation

A. General Principle: Although neither a corporation nor an individual target may avoid prosecution merely by paying a sum of money, a prosecutor may consider the corporation's willingness to make restitution and steps already taken to do so. A prosecutor may also consider other remedial actions, such as implementing an effective corporate compliance program, improving an existing compliance program, and disciplining wrongdoers, in determining whether to charge the corporation.

B. Comment: In determining whether or not a corporation should be prosecuted, a prosecutor may consider whether meaningful remedial measures have been taken, including employee discipline and full restitution.⁷ A corporation's response to misconduct says much about its willingness to ensure that such misconduct does not recur. Thus, corporations that fully recognize the seriousness of their misconduct and accept responsibility for it should be taking steps to implement the personnel, operational, and organizational changes necessary to establish an awareness among employees that criminal conduct will not be tolerated. Among the factors prosecutors should consider and weigh are whether the corporation appropriately disciplined the wrongdoers and disclosed information concerning their illegal conduct to the government.

Employee discipline is a difficult task for many corporations because of the human element involved and sometimes because of the seniority of the employees concerned. While corporations need to be fair to their employees, they must also be unequivocally committed, at all levels of the corporation, to the highest standards of legal and ethical behavior. Effective internal discipline can be a powerful deterrent against improper behavior by a

corporation's employees. In evaluating a corporation's response to wrongdoing, prosecutors may evaluate the willingness of the corporation to discipline culpable employees of all ranks and the adequacy of the discipline imposed. The prosecutor should be satisfied that the corporation's focus is on the integrity and credibility of its remedial and disciplinary measures rather than on the protection of the wrongdoers.

In addition to employee discipline, two other factors used in evaluating a corporation's remedial efforts are restitution and reform. As with natural persons, the decision whether or not to prosecute should not depend upon the target's ability to pay restitution. A corporation's efforts to pay restitution even in advance of any court order is, however, evidence of its "acceptance of responsibility" and, consistent with the practices and policies of the appropriate Division of the Department entrusted with enforcing specific criminal laws, may be considered in determining whether to bring criminal charges. Similarly, although the inadequacy of a corporate compliance program is a factor to consider when deciding whether to charge a corporation, that corporation's quick recognition of the flaws in the program and its efforts to improve the program are also factors to consider.

IX. Charging a Corporation: Collateral Consequences

A. General Principle: Prosecutors may consider the collateral consequences of a corporate criminal conviction in determining whether to charge the corporation with a criminal offense.

B. Comment: One of the factors in determining whether to charge a natural person or a corporation is whether the likely punishment is appropriate given the nature and seriousness of the crime. In the corporate context, prosecutors may take into account the possibly substantial consequences to a corporation's officers, directors, employees, and shareholders, many of whom may, depending on the size and nature (e.g., publicly vs. closely held) of the corporation and their role in its operations, have played no role in the criminal conduct, have been completely unaware of it, or have been wholly unable to prevent it. Prosecutors should also be aware of non-penal sanctions that may accompany a criminal charge, such as potential suspension or debarment from eligibility for government contracts or federal funded programs such as health care. Whether or not such non-penal sanctions are appropriate or required in a particular case is the responsibility of the relevant agency, a decision that will be made based on the applicable statutes, regulations, and policies.

Virtually every conviction of a corporation, like virtually every conviction of an individual, will have an impact on innocent third parties, and the mere existence of such an effect is not sufficient to preclude prosecution of the corporation. Therefore, in evaluating the severity of collateral consequences, various factors already discussed, such as the pervasiveness of the criminal conduct and the adequacy of the corporation's compliance programs, should be considered in determining the weight to be given to this factor. For instance, the balance may tip in favor of prosecuting corporations in situations where the scope of the misconduct in a case is widespread and sustained within a corporate division (or spread throughout pockets of the corporate organization). In such cases, the possible unfairness of visiting punishment for the corporation's crimes upon shareholders may be of much less concern where those shareholders have substantially profited, even unknowingly, from widespread or pervasive criminal activity. Similarly, where the top layers of the corporation's management or the shareholders of a closely-held corporation were engaged in or aware of the wrongdoing and the conduct at issue was accepted as a way of doing business for an extended period, debarment may be deemed not collateral, but a direct and entirely appropriate consequence of the corporation's wrongdoing.

The appropriateness of considering such collateral consequences and the weight to be given them may depend on the special policy concerns discussed in section III, *supra*.

X. Charging a Corporation: Non-Criminal Alternatives

A. General Principle: Although non-criminal alternatives to prosecution often exist, prosecutors may consider whether such sanctions would adequately deter, punish, and rehabilitate a corporation that has engaged in wrongful conduct. In evaluating the adequacy of non-criminal alternatives to prosecution, e.g., civil or regulatory enforcement actions, the prosecutor may consider all relevant factors, including:

1. the sanctions available under the alternative means of disposition;
2. the likelihood that an effective sanction will be imposed; and

3. the effect of non-criminal disposition on Federal law enforcement interests.

B. Comment: The primary goals of criminal law are deterrence, punishment, and rehabilitation. Non-criminal sanctions may not be an appropriate response to an egregious violation, a pattern of wrongdoing, or a history of non-criminal sanctions without proper remediation. In other cases, however, these goals may be satisfied without the necessity of instituting criminal proceedings. In determining whether federal criminal charges are appropriate, the prosecutor should consider the same factors (modified appropriately for the regulatory context) considered when determining whether to leave prosecution of a natural person to another jurisdiction or to seek non-criminal alternatives to prosecution. These factors include: the strength of the regulatory authority's interest; the regulatory authority's ability and willingness to take effective enforcement action; the probable sanction if the regulatory authority's enforcement action is upheld; and the effect of a non-criminal disposition on Federal law enforcement interests. See USAM §§ 9-27.240, 9-27.250.

XI. Charging a Corporation: Selecting Charges

A. General Principle: Once a prosecutor has decided to charge a corporation, the prosecutor should charge, or should recommend that the grand jury charge, the most serious offense that is consistent with the nature of the defendant's conduct and that is likely to result in a sustainable conviction.

B. Comment: Once the decision to charge is made, the same rules as govern charging natural persons apply. These rules require "a faithful and honest application of the Sentencing Guidelines" and an "individualized assessment of the extent to which particular charges fit the specific circumstances of the case, are consistent with the purposes of the Federal criminal code, and maximize the impact of Federal resources on crime." See USAM § 9-27.300. In making this determination, "it is appropriate that the attorney for the government consider, *inter alia*, such factors as the sentencing guideline range yielded by the charge, whether the penalty yielded by such sentencing range ... is proportional to the seriousness of the defendant's conduct, and whether the charge achieves such purposes of the criminal law as punishment, protection of the public, specific and general deterrence, and rehabilitation." See Attorney General's Memorandum, dated October 12, 1993.

XII. Plea Agreements with Corporations

A. General Principle: In negotiating plea agreements with corporations, prosecutors should seek a plea to the most serious, readily provable offense charged. In addition, the terms of the plea agreement should contain appropriate provisions to ensure punishment, deterrence, rehabilitation, and compliance with the plea agreement in the corporate context. Although special circumstances may mandate a different conclusion, prosecutors generally should not agree to accept a corporate guilty plea in exchange for non-prosecution or dismissal of charges against individual officers and employees.

B. Comment: Prosecutors may enter into plea agreements with corporations for the same reasons and under the same constraints as apply to plea agreements with natural persons. See USAM §§ 9-27.400-500. This means, *inter alia*, that the corporation should be required to plead guilty to the most serious, readily provable offense charged. As is the case with individuals, the attorney making this determination should do so "on the basis of an individualized assessment of the extent to which particular charges fit the specific circumstances of the case, are consistent with the purposes of the federal criminal code, and maximize the impact of federal resources on crime. In making this determination, the attorney for the government considers, *inter alia*, such factors as the sentencing guideline range yielded by the charge, whether the penalty yielded by such sentencing range ... is proportional to the seriousness of the defendant's conduct, and whether the charge achieves such purposes of the criminal law as punishment, protection of the public, specific and general deterrence, and rehabilitation." See Attorney General's Memorandum, dated October 12, 1993. In addition, any negotiated departures from the Sentencing Guidelines must be justifiable under the Guidelines and must be disclosed to the sentencing court. A corporation should be made to realize that pleading guilty to criminal charges constitutes an admission of guilt and not merely a resolution of an inconvenient distraction from its business. As with natural persons, pleas should be structured so that the corporation may not later "proclaim lack of culpability or even complete innocence." See USAM §§ 9-27.420(b)(4), 9-27.440, 9-27.500. Thus, for instance, there should be placed upon the record a sufficient factual basis for the plea to prevent later corporate assertions of innocence.

A corporate plea agreement should also contain provisions that recognize the nature of the corporate "person" and ensure that the principles of punishment, deterrence, and rehabilitation are met. In the corporate context, punishment and deterrence are generally accomplished by substantial fines, mandatory restitution, and

institution of appropriate compliance measures, including, if necessary, continued judicial oversight or the use of special masters. See USSG §§ 8B1.1, 8C2.1, *et seq.* In addition, where the corporation is a government contractor, permanent or temporary debarment may be appropriate. Where the corporation was engaged in government contracting fraud, a prosecutor may not negotiate away an agency's right to debar or to list the corporate defendant.

In negotiating a plea agreement, prosecutors should also consider the deterrent value of prosecutions of individuals within the corporation. Therefore, one factor that a prosecutor may consider in determining whether to enter into a plea agreement is whether the corporation is seeking immunity for its employees and officers or whether the corporation is willing to cooperate in the investigation of culpable individuals. Prosecutors should rarely negotiate away individual criminal liability in a corporate plea.

Rehabilitation, of course, requires that the corporation undertake to be law-abiding in the future. It is, therefore, appropriate to require the corporation, as a condition of probation, to implement a compliance program or to reform an existing one. As discussed above, prosecutors may consult with the appropriate state and federal agencies and components of the Justice Department to ensure that a proposed compliance program is adequate and meets industry standards and best practices. See section VII, *supra*.

In plea agreements in which the corporation agrees to cooperate, the prosecutor should ensure that the cooperation is complete and truthful. To do so, the prosecutor may request that the corporation waive attorney-client and work product protection, make employees and agents available for debriefing, disclose the results of its internal investigation, file appropriate certified financial statements, agree to governmental or third-party audits, and take whatever other steps are necessary to ensure that the full scope of the corporate wrongdoing is disclosed and that the responsible culprits are identified and, if appropriate, prosecuted. See generally section VIII, *supra*.

Footnotes:

1. While these guidelines refer to corporations, they apply to the consideration of the prosecution of all types of business organizations, including partnerships, sole proprietorships, government entities, and unincorporated associations.
2. In addition, the Sentencing Guidelines reward voluntary disclosure and cooperation with a reduction in the corporation's offense level. See USSG §8C2.5(g).
3. This waiver should ordinarily be limited to the factual internal investigation and any contemporaneous advice given to the corporation concerning the conduct at issue. Except in unusual circumstances, prosecutors should not seek a waiver with respect to communications and work product related to advice concerning the government's criminal investigation.
4. Some states require corporations to pay the legal fees of officers under investigation prior to a formal determination of their guilt. Obviously, a corporation's compliance with governing law should not be considered a failure to cooperate.
5. Although this case and *Basic Construction* are both antitrust cases, their reasoning applies to other criminal violations. In the Hilton case, for instance, the Ninth Circuit noted that Sherman Act violations are commercial offenses "usually motivated by a desire to enhance profits," thus, bringing the case within the normal rule that a "purpose to benefit the corporation is necessary to bring the agent's acts within the scope of his employment." 467 F.2d at 1006 & n4. In addition, in *United States v. Automated Medical Laboratories*, 770 F.2d 399, 406 n.5 (4th Cir. 1985), the Fourth Circuit stated "that *Basic Construction* states a generally applicable rule on corporate criminal liability despite the fact that it addresses violations of the antitrust laws."
6. For a detailed review of these and other factors concerning corporate compliance programs, see United States Sentencing Commission, GUIDELINES MANUAL, §8A1.2, comment. (n.3(k)) (Nov. 1997). See also USSG §8C2.5(f)
7. For example, the Antitrust Division's amnesty policy requires that "[w]here possible, the corporation [make] restitution to injured parties...."

Appendix B



U.S. Department of Justice

Office of the Deputy Attorney General

The Deputy Attorney General

Washington, D.C. 20530

MEMORANDUM

TO: Heads of Department Components
United States Attorneys

FROM: Paul J. McNulty
Deputy Attorney General

SUBJECT: Principles of Federal Prosecution of Business Organizations

The Department experienced unprecedented success in prosecuting corporate fraud during the last four years. We have aggressively rooted out corruption in financial markets and corporate board rooms across the country. Federal prosecutors should be justifiably proud that the information used by our nation's financial markets is more reliable, our retirement plans are more secure, and the investing public is better protected as a result of our efforts. The most significant result of this enforcement initiative is that corporations increasingly recognize the need for self-policing, self-reporting, and cooperation with law enforcement. Through their self-regulation efforts, fraud undoubtedly is being prevented, sparing shareholders from the financial harm accompanying corporate corruption. The Department must continue to encourage these efforts.

Though much has been accomplished, the work of protecting the integrity of the marketplace continues. As we press forward in our enforcement duties, it is appropriate that we consider carefully proposals which could make our efforts more effective. I remain convinced that the fundamental principles that have guided our enforcement practices are sound. In particular, our corporate charging principles are not only familiar, but they are welcomed by most corporations in our country because good corporate leadership shares many of our goals. Like federal prosecutors, corporate leaders must take action to protect shareholders, preserve corporate value, and promote honesty and fair dealing with the investing public.

We have heard from responsible corporate officials recently about the challenges they face in discharging their duties to the corporation while responding in a meaningful way to a government investigation. Many of those associated with the corporate legal community have expressed concern that our practices may be discouraging full and candid communications between corporate employees and legal counsel. To the extent this is happening, it was never the intention of the Department for our corporate charging principles to cause such a result.

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Therefore, I have decided to adjust certain aspects of our policy in ways that will further promote public confidence in the Department, encourage corporate fraud prevention efforts, and clarify our goals without sacrificing our ability to prosecute these important cases effectively. The new language expands upon the Department's long-standing policies concerning how we evaluate the authenticity of a corporation's cooperation with a government investigation.

This memorandum supersedes and replaces guidance contained in the Memorandum from Deputy Attorney General Larry D. Thompson entitled Principles of Federal Prosecution of Business Organizations (January 20, 2003) (the "Thompson Memorandum") and the Memorandum from the Acting Deputy Attorney General Robert D. McCallum, Jr. entitled Waiver of Corporate Attorney-Client and Work Product Protections (October 21, 2005) (the "McCallum Memorandum").



U.S. Department of Justice

Office of the Deputy Attorney General

The Deputy Attorney General

Washington, D.C. 20530

MEMORANDUM

TO: Heads of Department Components
United States Attorneys

FROM: Paul J. McNulty
Deputy Attorney General

SUBJECT: Principles of Federal Prosecution of Business Organizations

Federal Prosecution of Business Organizations¹

I. Duties of the Federal Prosecutor; Duties of Corporate Leaders

The prosecution of corporate crime is a high priority for the Department of Justice. By investigating wrongdoing and bringing charges for criminal conduct, the Department plays an important role in protecting investors and ensuring public confidence in business entities and in the investment markets in which those entities participate. In this respect, federal prosecutors and corporate leaders share a common goal. Directors and officers owe a fiduciary duty to a corporation's shareholders, the corporation's true owners, and they owe duties of honest dealing to the investing public in connection with the corporation's regulatory filings and public statements. The faithful execution of these duties by corporate leadership serves the same values in promoting public trust and confidence that our criminal prosecutions are designed to serve.

A prosecutor's duty to enforce the law requires the investigation and prosecution of criminal wrongdoing if it is discovered. In carrying out this mission with the diligence and resolve necessary to vindicate the important public interests discussed above, prosecutors should be mindful of the common cause we share with responsible corporate leaders. Prosecutors should also be mindful that confidence in the Department is affected both by the results we achieve and by the real and perceived ways in which we achieve them. Thus, the manner in

¹ While these guidelines refer to corporations, they apply to the consideration of the prosecution of all types of business organizations, including partnerships, sole proprietorships, government entities, and unincorporated associations.

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which we do our job as prosecutors – the professionalism we demonstrate, our resourcefulness in seeking information, and our willingness to secure the facts in a manner that encourages corporate compliance and self-regulation – impacts public perception of our mission. Federal prosecutors recognize that they must maintain public confidence in the way in which they exercise their charging discretion, and that professionalism and civility have always played an important part in putting these principles into action.

II. Charging a Corporation: General Principles

A. General Principle: Corporations should not be treated leniently because of their artificial nature nor should they be subject to harsher treatment. Vigorous enforcement of the criminal laws against corporate wrongdoers, where appropriate, results in great benefits for law enforcement and the public, particularly in the area of white collar crime. Indicting corporations for wrongdoing enables the government to address and be a force for positive change of corporate culture, alter corporate behavior, and prevent, discover, and punish white collar crime.

B. Comment: In all cases involving corporate wrongdoing, prosecutors should consider the factors discussed herein. First and foremost, prosecutors should be aware of the important public benefits that may flow from indicting a corporation in appropriate cases. For instance, corporations are likely to take immediate remedial steps when one is indicted for criminal conduct that is pervasive throughout a particular industry, and thus an indictment often provides a unique opportunity for deterrence on a massive scale. In addition, a corporate indictment may result in specific deterrence by changing the culture of the indicted corporation and the behavior of its employees. Finally, certain crimes that carry with them a substantial risk of great public harm, e.g., environmental crimes or financial frauds, are by their nature most likely to be committed by businesses, and there may, therefore, be a substantial federal interest in indicting the corporation.

Charging a corporation, however, does not mean 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, even in the face of an offer of a corporate guilty plea or some other disposition of the charges against the corporation.

Corporations are "legal persons," capable of suing and being sued, and capable of committing crimes. Under the doctrine of *respondeat superior*, a corporation may be held criminally liable for the illegal acts of its directors, officers, employees, and agents. To hold a corporation liable for these actions, the government must establish that the corporate agent's actions (i) were within the scope of his duties and (ii) were intended, at least in part, to benefit the corporation. In all cases involving wrongdoing by corporate agents, prosecutors should consider the corporation, as well as the responsible individuals, as potential criminal targets.

Agents, however, may act for mixed reasons -- both for self-aggrandizement (both direct and indirect) and for the benefit of the corporation, and a corporation may be held liable as long as one motivation of its agent is to benefit the corporation. See *United States v. Potter*, 463 F.3d 9, 25 (1st Cir. 2006) (stating that the test to determine whether an agent is acting within the scope of employment is whether the agent is performing acts of the kind which he is authorized to perform, and those acts are motivated--at least in part--by an intent to benefit the corporation). In *United States v. Automated Medical Laboratories*, 770 F.2d 399 (4th Cir. 1985), the Fourth Circuit affirmed a corporation's conviction for the actions of a subsidiary's employee despite its claim that the employee was acting for his own benefit, namely his "ambitious nature and his desire to ascend the corporate ladder." The court stated, "*Partucci* was clearly acting in part to benefit AML since his advancement within the corporation depended on AML's well-being and its lack of difficulties with the FDA." Furthermore, in *United States v. Sun-Diamond Growers of California*, 138 F.3d 961, 969-70 (D.C. Cir. 1998), *aff'd on other grounds*, 526 U.S. 398 (1999), the D.C. Circuit rejected a corporation's argument that it should not be held criminally liable for the actions of its vice-president since the vice-president's "scheme was designed to -- and did in fact -- defraud [the corporation], not benefit it." According to the court, the fact that the vice-president deceived the corporation and used its money to contribute illegally to a congressional campaign did not preclude a valid finding that he acted to benefit the corporation. Part of the vice-president's job was to cultivate the corporation's relationship with the congressional candidate's brother, the Secretary of Agriculture. Therefore, the court held, the jury was entitled to conclude that the vice-president had acted with an intent, "however befuddled," to further the interests of his employer. See also *United States v. Cincotta*, 689 F.2d 238, 241-42 (1st Cir. 1982) (upholding a corporation's conviction, notwithstanding the substantial personal benefit reaped by its miscreant agents, because the fraudulent scheme required money to pass through the corporation's treasury and the fraudulently obtained goods were resold to the corporation's customers in the corporation's name).

Moreover, the corporation need not even necessarily profit from its agent's actions for it to be held liable. In *Automated Medical Laboratories*, the Fourth Circuit stated:

[B]enefit is not a "touchstone of criminal corporate liability; benefit at best is an evidential, not an operative, fact." Thus, whether the agent's actions ultimately redounded to the benefit of the corporation is less significant than whether the agent acted with the intent to benefit the corporation. The basic purpose of requiring that an agent have acted with the intent to benefit the corporation, however, is to insulate the corporation from criminal liability for actions of its agents which may be inimical to the interests of the corporation or which may have been undertaken solely to advance the interests of that agent or of a party other than the corporation.

770 F.2d at 407 (emphasis added; quoting *Old Monastery Co. v. United States*, 147 F.2d 905, 908 (4th Cir.), *cert. denied*, 326 U.S. 734 (1945)).

III. Charging a Corporation: Factors to Be Considered

A. General Principle: Generally, prosecutors apply the same factors in determining whether to charge a corporation as they do with respect to individuals. *See* USAM § 9-27.220, *et seq.* Thus, the prosecutor must weigh all of the factors normally considered in the sound exercise of prosecutorial judgment: the sufficiency of the evidence; the likelihood of success at trial; the probable deterrent, rehabilitative, and other consequences of conviction; and the adequacy of noncriminal approaches. *See id.* However, due to the nature of the corporate "person," some additional factors are present. In conducting an investigation, determining whether to bring charges, and negotiating plea agreements, prosecutors must consider the following factors in reaching a decision as to the proper treatment of a corporate target:

1. the nature and seriousness of the offense, including the risk of harm to the public, and applicable policies and priorities, if any, governing the prosecution of corporations for particular categories of crime (*see* section IV, *infra*);
2. the pervasiveness of wrongdoing within the corporation, including the complicity in, or condonation of, the wrongdoing by corporate management (*see* section V, *infra*);
3. the corporation's history of similar conduct, including prior criminal, civil, and regulatory enforcement actions against it (*see* section VI, *infra*);
4. the corporation's timely and voluntary disclosure of wrongdoing and its willingness to cooperate in the investigation of its agents (*see* section VII, *infra*);
5. the existence and adequacy of the corporation's pre-existing compliance program (*see* section VIII, *infra*);
6. the corporation's remedial actions, including any efforts to implement an effective corporate compliance program or to improve an existing one, to replace responsible management, to discipline or terminate wrongdoers, to pay restitution, and to cooperate with the relevant government agencies (*see* section IX, *infra*);
7. collateral consequences, including disproportionate harm to shareholders, pension holders and employees not proven personally culpable and impact on the public arising from the prosecution (*see* section X, *infra*);
8. the adequacy of the prosecution of individuals responsible for the corporation's malfeasance; and
9. the adequacy of remedies such as civil or regulatory enforcement actions (*see* section XI, *infra*).

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B. Comment: In determining whether to charge a corporation, the foregoing factors must be considered. The factors listed in this section are intended to be illustrative of those that should be considered and not a complete or exhaustive list. Some or all of these factors may or may not apply to specific cases, and in some cases one factor may override all others. For example, the nature and seriousness of the offense may be such as to warrant prosecution regardless of the other factors. In most cases, however, no single factor will be dispositive. Further, national law enforcement policies in various enforcement areas may require that more or less weight be given to certain of these factors than to others. Of course, prosecutors must exercise their judgment in applying and balancing these factors and this process does not mandate a particular result.

In making a decision to charge a corporation, the prosecutor generally has wide latitude in determining when, whom, how, and even whether to prosecute for violations of federal criminal law. In exercising that discretion, prosecutors should consider the following general statements of principles that summarize appropriate considerations to be weighed and desirable practices to be followed in discharging their prosecutorial responsibilities. In doing so, prosecutors should ensure that the general purposes of the criminal law -- assurance of warranted punishment, deterrence of further criminal conduct, protection of the public from dangerous and fraudulent conduct, rehabilitation of offenders, and restitution for victims and affected communities -- are adequately met, taking into account the special nature of the corporate "person."

IV. Charging a Corporation: Special Policy Concerns

A. General Principle: The nature and seriousness of the crime, including the risk of harm to the public from the criminal conduct, are obviously primary factors in determining whether to charge a corporation. In addition, corporate conduct, particularly that of national and multi-national corporations, necessarily intersects with federal economic, taxation, and criminal law enforcement policies. In applying these principles, prosecutors must consider the practices and policies of the appropriate Division of the Department, and must comply with those policies to the extent required.

B. Comment: In determining whether to charge a corporation, prosecutors should take into account federal law enforcement priorities as discussed above. See USAM § 9-27-230. In addition, however, prosecutors must be aware of the specific policy goals and incentive programs established by the respective Divisions and regulatory agencies. Thus, whereas natural persons may be given incremental degrees of credit (ranging from immunity to lesser charges to sentencing considerations) for turning themselves in, making statements against their penal interest, and cooperating in the government's investigation of their own and others' wrongdoing, the same approach may not be appropriate in all circumstances with respect to corporations. As an example, it is entirely proper in many investigations for a prosecutor to consider the corporation's pre-indictment conduct, e.g., voluntary disclosure, cooperation, remediation or restitution, in determining whether to seek an indictment. However, this would not necessarily be appropriate in an antitrust investigation, in which antitrust violations, by definition, go to the

heart of the corporation's business and for which the Antitrust Division has therefore established a firm policy, understood in the business community, that credit should not be given at the charging stage for a compliance program and that amnesty is available only to the first corporation to make full disclosure to the government. As another example, the Tax Division has a strong preference for prosecuting responsible individuals, rather than entities, for corporate tax offenses. Thus, in determining whether or not to charge a corporation, prosecutors must consult with the Criminal, Antitrust, Tax, and Environmental and Natural Resources Divisions, if appropriate or required.

V. Charging a Corporation: Pervasiveness of Wrongdoing Within the Corporation

A. General Principle: A corporation can only act through natural persons, and it is therefore held responsible for the acts of such persons fairly attributable to it. Charging a corporation for even minor misconduct may be appropriate where the wrongdoing was pervasive and was undertaken by a large number of employees or by all the employees in a particular role within the corporation, *e.g.*, salesmen or procurement officers, or was condoned by upper management. On the other hand, in certain limited circumstances, it may not be appropriate to impose liability upon a corporation, particularly one with a compliance program in place, under a strict *respondeat superior* theory for the single isolated act of a rogue employee. There is, of course, a wide spectrum between these two extremes, and a prosecutor should exercise sound discretion in evaluating the pervasiveness of wrongdoing within a corporation.

B. Comment: Of these factors, the most important is the role of management. Although acts of even low-level employees may result in criminal liability, a corporation is directed by its management and management is responsible for a corporate culture in which criminal conduct is either discouraged or tacitly encouraged. As stated in commentary to the Sentencing Guidelines:

Pervasiveness [is] case specific and [will] depend on the number, and degree of responsibility, of individuals [with] substantial authority ... who participated in, condoned, or were willfully ignorant of the offense. Fewer individuals need to be involved for a finding of pervasiveness if those individuals exercised a relatively high degree of authority. Pervasiveness can occur either within an organization as a whole or within a unit of an organization. *See* USSG §8C2.5, comment. (n. 4).

VI. Charging a Corporation: The Corporation's Past History

A. General Principle: Prosecutors may consider a corporation's history of similar conduct, including prior criminal, civil, and regulatory enforcement actions against it, in determining whether to bring criminal charges.

B. Comment: A corporation, like a natural person, is expected to learn from its mistakes. A history of similar conduct may be probative of a corporate culture that encouraged, or at least condoned, such conduct, regardless of any compliance programs. Criminal prosecution of a

corporation may be particularly appropriate where the corporation previously had been subject to non-criminal guidance, warnings, or sanctions, or previous criminal charges, and it either had not taken adequate action to prevent future unlawful conduct or had continued to engage in the conduct in spite of the warnings or enforcement actions taken against it. In making this determination, the corporate structure itself, e.g. subsidiaries or operating divisions, should be ignored, and enforcement actions taken against the corporation or any of its divisions, subsidiaries, and affiliates should be considered. See USSG § 8C2.5(c) & comment.(n. 6).

VII. Charging a Corporation: The Value of Cooperation

A. General Principle: In determining whether to charge a corporation, that corporation's timely and voluntary disclosure of wrongdoing and its cooperation with the government's investigation may be relevant factors. In 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 evidence and to identify the culprits within the corporation, including senior executives.

B. Comment: In investigating wrongdoing by or within a corporation, a prosecutor is likely to encounter several obstacles resulting from the nature of the corporation itself. It will often be difficult to determine which individual took which action on behalf of the corporation. Lines of authority and responsibility may be shared among operating divisions or departments, and records and personnel may be spread throughout the United States or even among several countries. Where the criminal conduct continued over an extended period of time, the culpable or knowledgeable personnel may have been promoted, transferred, or fired, or they may have quit or retired. Accordingly, a corporation's cooperation may be critical in identifying the culprits and locating relevant evidence. Relevant considerations in determining whether a corporation has cooperated are set forth below.

1. Qualifying for Immunity, Amnesty or Pretrial Diversion

In some circumstances, granting a corporation immunity or amnesty or pretrial diversion may be considered in the course of the government's investigation. In such circumstances, prosecutors should refer to the principles governing non-prosecution agreements generally. See USAM § 9-27.600-650. These principles permit a non-prosecution agreement in exchange for cooperation when a corporation's "timely cooperation appears to be necessary to the public interest and other means of obtaining the desired cooperation are unavailable or would not be effective." Prosecutors should note that in the case of national or multi-national corporations, multi-district or global agreements may be necessary. Such agreements may only be entered into with the approval of each affected district or the appropriate Department official. See USAM §9-27.641.

In addition, the Department, in conjunction with regulatory agencies and other executive branch departments, encourages corporations, as part of their compliance programs, to conduct internal investigations and to disclose their findings to the appropriate authorities. Some agencies, such as the Securities and Exchange Commission and the Environmental Protection Agency, as well as the Department's Environmental and Natural Resources Division, have formal voluntary disclosure programs in which self-reporting, coupled with remediation and additional criteria, may qualify the corporation for amnesty or reduced sanctions. Even in the absence of a formal program, prosecutors may consider a corporation's timely and voluntary disclosure in evaluating the adequacy of the corporation's compliance program and its management's commitment to the compliance program. However, prosecution and economic policies specific to the industry or statute may require prosecution notwithstanding a corporation's willingness to cooperate. For example, the Antitrust Division offers amnesty only to the first corporation to agree to cooperate. This creates a strong incentive for corporations participating in anti-competitive conduct to be the first to cooperate. In addition, amnesty, immunity, or reduced sanctions may not be appropriate where the corporation's business is permeated with fraud or other crimes.

2. Waiving Attorney-Client and Work Product Protections²

The attorney-client and work product protections serve an extremely important function in the U.S. legal system. The attorney-client privilege is one of the oldest and most sacrosanct privileges under U.S. law. *See Upjohn v. United States*, 449 U.S. 383, 389 (1976). As the Supreme Court has stated "its purpose is to encourage full and frank communication between attorneys and their clients and thereby promote broader public interests in the observance of law and administration of justice." *Id.* The work product doctrine also serves similarly important interests.

Waiver of attorney-client and work product protections is not a prerequisite to a finding that a company has cooperated in the government's investigation. However, a company's disclosure of privileged information may permit the government to expedite its investigation. In addition, the disclosure of privileged information may be critical in enabling the government to evaluate the accuracy and completeness of the company's voluntary disclosure.

Prosecutors may only request waiver of attorney-client or work product protections when there is a legitimate need for the privileged information to fulfill their law enforcement obligations. A legitimate need for the information is not established by concluding it is merely

² The Sentencing Guidelines reward voluntary disclosure and cooperation with a reduction in the corporation's offense level. *See* USSG §8C2.5(g). The reference to consideration of a corporation's waiver of attorney-client and work product protections in reducing a corporation's culpability score in Application Note 12, was deleted effective November 1, 2006. *See* USSG §8C2.5(g), comment. (n.12).

desirable or convenient to obtain privileged information. The test requires a careful balancing of important policy considerations underlying the attorney-client privilege and work product doctrine and the law enforcement needs of the government's investigation.

Whether there is a legitimate need depends upon:

- (1) the likelihood and degree to which the privileged information will benefit the government's investigation;
- (2) whether the information sought can be obtained in a timely and complete fashion by using alternative means that do not require waiver;
- (3) the completeness of the voluntary disclosure already provided; and
- (4) the collateral consequences to a corporation of a waiver.

If a legitimate need exists, prosecutors should seek the least intrusive waiver necessary to conduct a complete and thorough investigation, and should follow a step-by-step approach to requesting information. Prosecutors should first request purely factual information, which may or may not be privileged, relating to the underlying misconduct ("Category I"). Examples of Category I information could include, without limitation, copies of key documents, witness statements, or purely factual interview memoranda regarding the underlying misconduct, organization charts created by company counsel, factual chronologies, factual summaries, or reports (or portions thereof) containing investigative facts documented by counsel.

Before requesting that a corporation waive the attorney-client or work product protections for Category I information, prosecutors must obtain written authorization from the United States Attorney who must provide a copy of the request to, and consult with, the Assistant Attorney General for the Criminal Division before granting or denying the request. A prosecutor's request to the United States Attorney for authorization to seek a waiver must set forth law enforcement's legitimate need for the information and identify the scope of the waiver sought. A copy of each waiver request and authorization for Category I information must be maintained in the files of the United States Attorney. If the request is authorized, the United States Attorney must communicate the request in writing to the corporation.

A corporation's response to the government's request for waiver of privilege for Category I information may be considered in determining whether a corporation has cooperated in the government's investigation.

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Only if the purely factual information provides an incomplete basis to conduct a thorough investigation should prosecutors then request that the corporation provide attorney-client communications or non-factual attorney work product ("Category II"). This information includes legal advice given to the corporation before, during, and after the underlying misconduct occurred.

This category of privileged information might include the production of attorney notes, memoranda or reports (or portions thereof) containing counsel's mental impressions and conclusions, legal determinations reached as a result of an internal investigation, or legal advice given to the corporation.

Prosecutors are cautioned that Category II information should only be sought in rare circumstances.

Before requesting that a corporation waive the attorney-client or work product protections for Category II information, the United States Attorney must obtain written authorization from the Deputy Attorney General. A United States Attorney's request for authorization to seek a waiver must set forth law enforcement's legitimate need for the information and identify the scope of the waiver sought. A copy of each waiver request and authorization for Category II information must be maintained in the files of the Deputy Attorney General. If the request is authorized, the United States Attorney must communicate the request in writing to the corporation.

If a corporation declines to provide a waiver for Category II information after a written request from the United States Attorney, prosecutors must not consider this declination against the corporation in making a charging decision. Prosecutors may always favorably consider a corporation's acquiescence to the government's waiver request in determining whether a corporation has cooperated in the government's investigation.

Requests for Category II information requiring the approval of the Deputy Attorney General do not include:

- (1) legal advice contemporaneous to the underlying misconduct when the corporation or one of its employees is relying upon an advice-of-counsel defense; and
- (2) legal advice or communications in furtherance of a crime or fraud, coming within the crime-fraud exception to the attorney-client privilege.

In these two instances, prosecutors should follow the authorization process established for requesting waiver for Category I information.

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For federal prosecutors in litigating Divisions within Main Justice, waiver requests for Category I information must be submitted for approval to the Assistant Attorney General of the Division and waiver requests for Category II information must be submitted by the Assistant Attorney General for approval to the Deputy Attorney General. If the request is authorized, the Assistant Attorney General must communicate the request in writing to the corporation.

Federal prosecutors are not required to obtain authorization if the corporation voluntarily offers privileged documents without a request by the government. However, voluntary waivers must be reported to the United States Attorney or the Assistant Attorney General in the Division where the case originated. A record of these reports must be maintained in the files of that office.

3. Shielding Culpable Employees and Agents

Another factor to be weighed by the prosecutor is whether the corporation appears to be protecting its culpable employees and agents. Thus, while cases will differ depending on the circumstances, a corporation's promise of support to culpable employees and agents, *e.g.*, through retaining the employees without sanction for their misconduct or through providing information to the employees about the government's investigation pursuant to a joint defense agreement, may be considered by the prosecutor in weighing the extent and value of a corporation's cooperation.

Prosecutors generally should not take into account whether a corporation is advancing attorneys' fees to employees or agents under investigation and indictment. Many state indemnification statutes grant corporations the power to advance the legal fees of officers under investigation prior to a formal determination of guilt. As a consequence, many corporations enter into contractual obligations to advance attorneys' fees through provisions contained in their corporate charters, bylaws or employment agreements. Therefore, a corporation's compliance with governing state law and its contractual obligations cannot be considered a failure to cooperate.³ This prohibition is not meant to prevent a prosecutor from asking questions about an

³ In extremely rare cases, the advancement of attorneys' fees may be taken into account when the totality of the circumstances show that it was intended to impede a criminal investigation. In these cases, fee advancement is considered with many other telling facts to make a determination that the corporation is acting improperly to shield itself and its culpable employees from government scrutiny. *See discussion in Brief of Appellant-United States, United States v. Smith and Watson*, No. 06-3999-cr (2d Cir. Nov. 6, 2006). Where these circumstances exist, approval must be obtained from the Deputy Attorney General before prosecutors may consider this factor in their charging decisions. Prosecutors should follow the authorization process established for waiver requests of Category II information (see section VII-2, *infra*).

attorney's representation of a corporation or its employees.⁴

4. Obstructing the Investigation

Another factor to be weighed by the prosecutor is whether the corporation, while purporting to cooperate, has engaged in conduct intended to impede the investigation (whether or not rising to the level of criminal obstruction). Examples of such conduct include: overly broad assertions of corporate representation of employees or former employees; overly broad or frivolous assertions of privilege to withhold the disclosure of relevant, non-privileged documents; inappropriate directions to employees or their counsel, such as directions not to cooperate openly and fully with the investigation including, for example, the direction to decline to be interviewed; making presentations or submissions that contain misleading assertions or omissions; incomplete or delayed production of records; and failure to promptly disclose illegal conduct known to the corporation.

5. Offering Cooperation: No Entitlement to Immunity

Finally, a corporation's offer of cooperation does not automatically entitle it to immunity from prosecution. A corporation should not be able to escape liability merely by offering up its directors, officers, employees, or agents as in lieu of its own prosecution. Thus, a corporation's willingness to cooperate is merely one relevant factor, that needs to be considered in conjunction with the other factors, particularly those relating to the corporation's past history and the role of management in the wrongdoing.

VIII. Charging a Corporation: Corporate Compliance Programs

A. General Principle: Compliance programs are established by corporate management to prevent and to detect misconduct and to ensure that corporate activities are conducted in accordance with all applicable criminal and civil laws, regulations, and rules. The Department encourages such corporate self-policing, including voluntary disclosures to the government of any problems that a corporation discovers on its own. However, the existence of a compliance program is not sufficient, in and of itself, to justify not charging a corporation for criminal conduct undertaken by its officers, directors, employees, or agents. Indeed, the commission of such crimes in the face of a compliance program may suggest that the corporate management is

⁴ Routine questions regarding the representation status of a corporation and its employees, including how and by whom attorneys' fees are paid, frequently arise in the course of an investigation. They may be necessary to assess other issues, such as conflict-of-interest. Such questions are appropriate and this guidance is not intended to prohibit such inquiry.

not adequately enforcing its program. In addition, the nature of some crimes, *e.g.*, antitrust violations, may be such that national law enforcement policies mandate prosecutions of corporations notwithstanding the existence of a compliance program.

B. Comment: A corporate compliance program, even one specifically prohibiting the very conduct in question, does not absolve the corporation from criminal liability under the doctrine of *respondeat superior*. See *United States v. Basic Construction Co.*, 711 F.2d 570 (4th Cir. 1983) ("[A] corporation may be held criminally responsible for antitrust violations committed by its employees if they were acting within the scope of their authority, or apparent authority, and for the benefit of the corporation, even if... such acts were against corporate policy or express instructions."). In *United States v. Potter*, 463 F.3d 9, 25-26 (1st Cir. According to the court, a corporation cannot "avoid liability by adopting abstract rules" that forbid its agents from engaging in illegal acts; "even a specific directive to an agent or employee or honest efforts to police such rules do not automatically free the company for the wrongful acts of agents." Similarly, in *United States v. Hilton Hotels Corp.*, 467 F.2d 1000 (9th Cir. 1972), *cert. denied*, 409 U.S. 1125 (1973), the Ninth Circuit affirmed antitrust liability based upon a purchasing agent for a single hotel threatening a single supplier with a boycott unless it paid dues to a local marketing association, even though the agent's actions were contrary to corporate policy and directly against express instructions from his superiors. The court reasoned that Congress, in enacting the Sherman Antitrust Act, "intended to impose liability upon business entities for the acts of those to whom they choose to delegate the conduct of their affairs, thus stimulating a maximum effort by owners and managers to assure adherence by such agents to the requirements of the Act."⁵ It concluded that "general policy statements" and even direct instructions from the agent's superiors were not sufficient; "Appellant could not gain exculpation by issuing general instructions without undertaking to enforce those instructions by means commensurate with the obvious risks." See also *United States v. Beusch*, 596 F.2d 871, 878 (9th Cir. 1979) ("[A] corporation may be liable for the acts of its employees done contrary to express instructions and policies, but ... the existence of such instructions and policies may be considered in determining whether the employee in fact acted to benefit the corporation."); *United States v. American Radiator & Standard Sanitary Corp.*, 433 F.2d 174 (3rd Cir. 1970) (affirming conviction of corporation based upon its officer's participation in price-fixing scheme, despite corporation's defense that officer's conduct violated its "rigid anti-fraternization policy" against any socialization (and exchange of price information) with its competitors; "When the act of the agent is within the scope of his employment or his apparent authority, the corporation is held

⁵ Although this case and *Basic Construction* are both antitrust cases, their reasoning applies to other criminal violations. In the *Hilton* case, for instance, the Ninth Circuit noted that Sherman Act violations are commercial offenses "usually motivated by a desire to enhance profits," thus, bringing the case within the normal rule that a "purpose to benefit the corporation is necessary to bring the agent's acts within the scope of his employment." 467 F.2d at 1006 & n4. In addition, in *United States v. Automated Medical Laboratories*, 770 F.2d 399, 406 n.5 (4th Cir. 1985), the Fourth Circuit stated "that *Basic Construction* states a generally applicable rule on corporate criminal liability despite the fact that it addresses violations of the antitrust laws."

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legally responsible for it, although what he did may be contrary to his actual instructions and may be unlawful.").

While the Department recognizes that no compliance program can ever prevent all criminal activity by a corporation's employees, the critical factors in evaluating any program are whether the program is adequately designed for maximum effectiveness in preventing and detecting wrongdoing by employees and whether corporate management is enforcing the program or is tacitly encouraging or pressuring employees to engage in misconduct to achieve business objectives. The Department has no formal guidelines for corporate compliance programs. The fundamental questions any prosecutor should ask are: "Is the corporation's compliance program well designed?" and "Does the corporation's compliance program work?" In answering these questions, the prosecutor should consider the comprehensiveness of the compliance program; the extent and pervasiveness of the criminal conduct; the number and level of the corporate employees involved; the seriousness, duration, and frequency of the misconduct; and any remedial actions taken by the corporation, including restitution, disciplinary action, and revisions to corporate compliance programs.⁶ Prosecutors should also consider the promptness of any disclosure of wrongdoing to the government and the corporation's cooperation in the government's investigation. In evaluating compliance programs, prosecutors may consider whether the corporation has established corporate governance mechanisms that can effectively detect and prevent misconduct. For example, do the corporation's directors exercise independent review over proposed corporate actions rather than unquestioningly ratifying officers' recommendations; are the directors provided with information sufficient to enable the exercise of independent judgment, are internal audit functions conducted at a level sufficient to ensure their independence and accuracy and have the directors established an information and reporting system in the organization reasonably designed to provide management and the board of directors with timely and accurate information sufficient to allow them to reach an informed decision regarding the organization's compliance with the law. *In re: Caremark*, 698 A.2d 959 (Del. Ct. Chan. 1996).

Prosecutors should therefore attempt to determine whether a corporation's compliance program is merely a "paper program" or whether it was designed and implemented in an effective manner. In addition, prosecutors should determine whether the corporation has provided for a staff sufficient to audit, document, analyze, and utilize the results of the corporation's compliance efforts. In addition, prosecutors should determine whether the corporation's employees are adequately informed about the compliance program and are convinced of the corporation's commitment to it. This will enable the prosecutor to make an informed decision as to whether the corporation has adopted and implemented a truly effective compliance program that, when consistent with other federal law enforcement policies, may result in a decision to charge only the corporation's employees and agents.

⁶ For a detailed review of these and other factors concerning corporate compliance programs, see USSG §8B2.1.

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Compliance programs should be designed to detect the particular types of misconduct most likely to occur in a particular corporation's line of business. Many corporations operate in complex regulatory environments outside the normal experience of criminal prosecutors. Accordingly, prosecutors should consult with relevant federal and state agencies with the expertise to evaluate the adequacy of a program's design and implementation. For instance, state and federal banking, insurance, and medical boards, the Department of Defense, the Department of Health and Human Services, the Environmental Protection Agency, and the Securities and Exchange Commission have considerable experience with compliance programs and can be very helpful to a prosecutor in evaluating such programs. In addition, the Fraud Section of the Criminal Division, the Commercial Litigation Branch of the Civil Division, and the Environmental Crimes Section of the Environment and Natural Resources Division can assist U.S. Attorneys' Offices in finding the appropriate agency office and in providing copies of compliance programs that were developed in previous cases.

IX. Charging a Corporation: Restitution and Remediation

A. **General Principle:** Although neither a corporation nor an individual target may avoid prosecution merely by paying a sum of money, a prosecutor may consider the corporation's willingness to make restitution and steps already taken to do so. A prosecutor may also consider other remedial actions, such as implementing an effective corporate compliance program, improving an existing compliance program, and disciplining wrongdoers, in determining whether to charge the corporation.

B. **Comment:** In determining whether or not a corporation should be prosecuted, a prosecutor may consider whether meaningful remedial measures have been taken, including employee discipline and full restitution. A corporation's response to misconduct says much about its willingness to ensure that such misconduct does not recur. Thus, corporations that fully recognize the seriousness of their misconduct and accept responsibility for it should be taking steps to implement the personnel, operational, and organizational changes necessary to establish an awareness among employees that criminal conduct will not be tolerated. Among the factors prosecutors should consider and weigh are whether the corporation appropriately disciplined the wrongdoers and disclosed information concerning their illegal conduct to the government.

Employee discipline is a difficult task for many corporations because of the human element involved and sometimes because of the seniority of the employees concerned. While corporations need to be fair to their employees, they must also be unequivocally committed, at all levels of the corporation, to the highest standards of legal and ethical behavior. Effective internal discipline can be a powerful deterrent against improper behavior by a corporation's employees. In evaluating a corporation's response to wrongdoing, prosecutors may evaluate the willingness of the corporation to discipline culpable employees of all ranks and the adequacy of the discipline imposed. The prosecutor should be satisfied that the corporation's focus is on the integrity and credibility of its remedial and disciplinary measures rather than on the protection of the wrongdoers.

In addition to employee discipline, two other factors used in evaluating a corporation's remedial efforts are restitution and reform. As with natural persons, the decision whether or not to prosecute should not depend upon the target's ability to pay restitution. A corporation's efforts to pay restitution even in advance of any court order is, however, evidence of its "acceptance of responsibility" and, consistent with the practices and policies of the appropriate Division of the Department entrusted with enforcing specific criminal laws, may be considered in determining whether to bring criminal charges. Similarly, although the inadequacy of a corporate compliance program is a factor to consider when deciding whether to charge a corporation, that corporation's quick recognition of the flaws in the program and its efforts to improve the program are also factors to consider.

X. Charging a Corporation: Collateral Consequences

A. General Principle: Prosecutors may consider the collateral consequences of a corporate criminal conviction in determining whether to charge the corporation with a criminal offense.

B. Comment: One of the factors in determining whether to charge a natural person or a corporation is whether the likely punishment is appropriate given the nature and seriousness of the crime. In the corporate context, prosecutors may take into account the possibly substantial consequences to a corporation's officers, directors, employees, and shareholders, many of whom may, depending on the size and nature (*e.g.*, publicly vs. closely held) of the corporation and their role in its operations, have played no role in the criminal conduct, have been completely unaware of it, or have been wholly unable to prevent it. Prosecutors should also be aware of non-penal sanctions that may accompany a criminal charge, such as potential suspension or debarment from eligibility for government contracts or federal funded programs such as health care. Whether or not such non-penal sanctions are appropriate or required in a particular case is the responsibility of the relevant agency, a decision that will be made based on the applicable statutes, regulations, and policies.

Virtually every conviction of a corporation, like virtually every conviction of an individual, will have an impact on innocent third parties, and the mere existence of such an effect is not sufficient to preclude prosecution of the corporation. Therefore, in evaluating the severity of collateral consequences, various factors already discussed, such as the pervasiveness of the criminal conduct and the adequacy of the corporation's compliance programs, should be considered in determining the weight to be given to this factor. For instance, the balance may tip in favor of prosecuting corporations in situations where the scope of the misconduct in a case is widespread and sustained within a corporate division (or spread throughout pockets of the corporate organization). In such cases, the possible unfairness of visiting punishment for the corporation's crimes upon shareholders may be of much less concern where those shareholders have substantially profited, even unknowingly, from widespread or pervasive criminal activity.

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Similarly, where the top layers of the corporation's management or the shareholders of a closely-held corporation were engaged in or aware of the wrongdoing and the conduct at issue was accepted as a way of doing business for an extended period, debarment may be deemed not collateral, but a direct and entirely appropriate consequence of the corporation's wrongdoing.

The appropriateness of considering such collateral consequences and the weight to be given them may depend on the special policy concerns discussed in section III, *supra*.

XI. Charging a Corporation: Non-Criminal Alternatives

A. General Principle: Non-criminal alternatives to prosecution often exist and prosecutors may consider whether such sanctions would adequately deter, punish, and rehabilitate a corporation that has engaged in wrongful conduct. In evaluating the adequacy of non-criminal alternatives to prosecution, e.g., civil or regulatory enforcement actions, the prosecutor may consider all relevant factors, including:

1. the sanctions available under the alternative means of disposition;
2. the likelihood that an effective sanction will be imposed; and
3. the effect of non-criminal disposition on federal law enforcement interests.

B. Comment: The primary goals of criminal law are deterrence, punishment, and rehabilitation. Non-criminal sanctions may not be an appropriate response to an egregious violation, a pattern of wrongdoing, or a history of non-criminal sanctions without proper remediation. In other cases, however, these goals may be satisfied without the necessity of instituting criminal proceedings. In determining whether federal criminal charges are appropriate, the prosecutor should consider the same factors (modified appropriately for the regulatory context) considered when determining whether to leave prosecution of a natural person to another jurisdiction or to seek non-criminal alternatives to prosecution. These factors include: the strength of the regulatory authority's interest; the regulatory authority's ability and willingness to take effective enforcement action; the probable sanction if the regulatory authority's enforcement action is upheld; and the effect of a non-criminal disposition on federal law enforcement interests. See USAM §§ 9-27.240, 9-27.250.

XII. Charging a Corporation: Selecting Charges

A. General Principle: Once a prosecutor has decided to charge a corporation, the prosecutor should charge, or should recommend that the grand jury charge, the most serious offense that is consistent with the nature of the defendant's conduct and that is likely to result in a sustainable conviction.

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B. Comment: Once the decision to charge is made, the same rules as govern charging natural persons apply. These rules require "a faithful and honest application of the Sentencing Guidelines" and an "individualized assessment of the extent to which particular charges fit the specific circumstances of the case, are consistent with the purposes of the federal criminal code, and maximize the impact of federal resources on crime." *See* USAM § 9-27.300. In making this determination, "it is appropriate that the attorney for the government consider, *inter alia*, such factors as the sentencing guideline range yielded by the charge, whether the penalty yielded by such sentencing range ... is proportional to the seriousness of the defendant's conduct, and whether the charge achieves such purposes of the criminal law as punishment, protection of the public, specific and general deterrence, and rehabilitation." *See* Attorney General's Memorandum, dated October 12, 1993.

XIII. Plea Agreements with Corporations

A. General Principle: In negotiating plea agreements with corporations, prosecutors should seek a plea to the most serious, readily provable offense charged. In addition, the terms of the plea agreement should contain appropriate provisions to ensure punishment, deterrence, rehabilitation, and compliance with the plea agreement in the corporate context. Although special circumstances may mandate a different conclusion, prosecutors generally should not agree to accept a corporate guilty plea in exchange for non-prosecution or dismissal of charges against individual officers and employees.

B. Comment: Prosecutors may enter into plea agreements with corporations for the same reasons and under the same constraints as apply to plea agreements with natural persons. *See* USAM §§ 9-27.400-500. This means, *inter alia*, that the corporation should be required to plead guilty to the most serious, readily provable offense charged. As is the case with individuals, the attorney making this determination should do so "on the basis of an individualized assessment of the extent to which particular charges fit the specific circumstances of the case, are consistent with the purposes of the federal criminal code, and maximize the impact of federal resources on crime. In making this determination, the attorney for the government considers, *inter alia*, such factors as the sentencing guideline range yielded by the charge, whether the penalty yielded by such sentencing range ... is proportional to the seriousness of the defendant's conduct, and whether the charge achieves such purposes of the criminal law as punishment, protection of the public, specific and general deterrence, and rehabilitation." *See* Attorney General's Memorandum, dated October 12, 1993. In addition, any negotiated departures from the Sentencing Guidelines must be justifiable under the Guidelines and must be disclosed to the sentencing court. A corporation should be made to realize that pleading guilty to criminal charges constitutes an admission of guilt and not merely a resolution of an inconvenient distraction from its business. As with natural persons, pleas should be structured so that the corporation may not later "proclaim lack of culpability or even complete innocence." *See* USAM §§ 9-27.420(b)(4), 9-27.440, 9-27.500. Thus, for instance, there should be placed upon the record a sufficient factual basis for the plea to prevent later corporate assertions of innocence.

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A corporate plea agreement should also contain provisions that recognize the nature of the corporate "person" and ensure that the principles of punishment, deterrence, and rehabilitation are met. In the corporate context, punishment and deterrence are generally accomplished by substantial fines, mandatory restitution, and institution of appropriate compliance measures, including, if necessary, continued judicial oversight or the use of special masters. *See* USSG §§ 8B1.1, 8C2.1, *et seq.* In addition, where the corporation is a government contractor, permanent or temporary debarment may be appropriate. Where the corporation was engaged in government contracting fraud, a prosecutor may not negotiate away an agency's right to debar or to list the corporate defendant.

In negotiating a plea agreement, prosecutors should also consider the deterrent value of prosecutions of individuals within the corporation. Therefore, one factor that a prosecutor may consider in determining whether to enter into a plea agreement is whether the corporation is seeking immunity for its employees and officers or whether the corporation is willing to cooperate in the investigation of culpable individuals. Prosecutors should rarely negotiate away individual criminal liability in a corporate plea.

Rehabilitation, of course, requires that the corporation undertake to be law-abiding in the future. It is, therefore, appropriate to require the corporation, as a condition of probation, to implement a compliance program or to reform an existing one. As discussed above, prosecutors may consult with the appropriate state and federal agencies and components of the Justice Department to ensure that a proposed compliance program is adequate and meets industry standards and best practices. *See* section VIII, *supra*.

In plea agreements in which the corporation agrees to cooperate, the prosecutor should ensure that the cooperation is complete and truthful. To do so, the prosecutor may request that the corporation waive attorney-client and work product protection, make employees and agents available for debriefing, disclose the results of its internal investigation, file appropriate certified financial statements, agree to governmental or third-party audits, and take whatever other steps are necessary to ensure that the full scope of the corporate wrongdoing is disclosed and that the responsible culprits are identified and, if appropriate, prosecuted. *See* generally section VII, *supra*.

This memorandum provides only internal Department of Justice guidance. It is not intended to, does not, and may not be relied upon to create any rights, substantive or procedural, enforceable at law by any party in any matter civil or criminal. Nor are any limitations hereby placed on otherwise lawful litigative prerogatives of the Department of Justice.

Appendix C

Title 9, Chapter 9-28.000

Principles of Federal Prosecution of Business Organizations

- 9-28.000 Principles of Federal Prosecution of Business Organizations
- 9-28.100 Duties of Federal Prosecutors and Duties of Corporate Leaders
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9-28.000 Principles of Federal Prosecution of Business Organizations¹

9-28.100 Duties of Federal Prosecutors and Duties of Corporate Leaders

The prosecution of corporate crime is a high priority for the Department of Justice. By investigating allegations of wrongdoing and by bringing charges where appropriate for criminal misconduct, the Department promotes critical public interests. These interests include, to take just a few examples: (1) protecting the integrity of our free economic and capital markets; (2) protecting consumers, investors, and business entities that compete only through lawful means; and (3) protecting the American people from misconduct that would violate criminal laws safeguarding the environment.

In this regard, federal prosecutors and corporate leaders typically share common goals. For example, directors and officers owe a fiduciary duty to a corporation's shareholders, the corporation's true owners, and they owe duties of honest dealing to the investing public in connection with the corporation's regulatory filings and public statements. The faithful execution of these duties by corporate leadership serves the same values in promoting public trust and confidence that our criminal cases are designed to serve.

A prosecutor's duty to enforce the law requires the investigation and prosecution of criminal wrongdoing if it is discovered. In carrying out this mission with the diligence and resolve necessary to vindicate the important public interests discussed above, prosecutors should be mindful of the common cause we share with responsible corporate leaders. Prosecutors should also be mindful that confidence in the Department is affected both by the results we achieve and by the real and perceived ways in which we achieve them. Thus, the manner in which we do our job as prosecutors—including the professionalism we demonstrate, our willingness to secure the facts in a manner that encourages corporate compliance and self-regulation, and also our appreciation that corporate prosecutions can potentially harm blameless investors, employees, and others—affects public perception of our mission. Federal prosecutors recognize that they must maintain public confidence in the way in which they exercise their charging discretion. This endeavor requires the thoughtful analysis of all facts and circumstances presented in a given case. As always, professionalism and civility play an important part in the Department's discharge of its responsibilities in all areas, including the area of corporate investigations and prosecutions.

9-28.200 General Considerations of Corporate Liability

A. General Principle: Corporations should not be treated leniently because of their artificial nature nor should they be subject to harsher treatment. Vigorous enforcement of the criminal laws against corporate wrongdoers, where appropriate, results in great benefits for law enforcement and the public, particularly in the area of white collar crime. Indicting corporations

¹ While these guidelines refer to corporations, they apply to the consideration of the prosecution of all types of business organizations, including partnerships, sole proprietorships, government entities, and unincorporated associations.

for wrongdoing enables the government to be a force for positive change of corporate culture, and a force to prevent, discover, and punish serious crimes.

B. Comment: In all cases involving corporate wrongdoing, prosecutors should consider the factors discussed further below. In doing so, prosecutors should be aware of the public benefits that can flow from indicting a corporation in appropriate cases. For instance, corporations are likely to take immediate remedial steps when one is indicted for criminal misconduct that is pervasive throughout a particular industry, and thus an indictment can provide a unique opportunity for deterrence on a broad scale. In addition, a corporate indictment may result in specific deterrence by changing the culture of the indicted corporation and the behavior of its employees. Finally, certain crimes that carry with them a substantial risk of great public harm—e.g., environmental crimes or sweeping financial frauds—may be committed by a business entity, and there may therefore be a substantial federal interest in indicting a corporation under such circumstances.

In certain instances, it may be appropriate, upon consideration of the factors set forth herein, to resolve a corporate criminal case by means other than indictment. Non-prosecution and deferred prosecution agreements, for example, occupy an important middle ground between declining prosecution and obtaining the conviction of a corporation. These agreements are discussed further in Section X, *infra*. Likewise, civil and regulatory alternatives may be appropriate in certain cases, as discussed in Section XI, *infra*.

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.

Corporations are “legal persons,” capable of suing and being sued, and capable of committing crimes. Under the doctrine of *respondeat superior*, a corporation may be held criminally liable for the illegal acts of its directors, officers, employees, and agents. To hold a corporation liable for these actions, the government must establish that the corporate agent’s actions (i) were within the scope of his duties and (ii) were intended, at least in part, to benefit the corporation. In all cases involving wrongdoing by corporate agents, prosecutors should not limit their focus solely to individuals or the corporation, but should consider both as potential targets.

Agents may act for mixed reasons—both for self-aggrandizement (both direct and indirect) and for the benefit of the corporation, and a corporation may be held liable as long as one motivation of its agent is to benefit the corporation. See *United States v. Potter*, 463 F.3d 9, 25 (1st Cir. 2006) (stating that the test to determine whether an agent is acting within the scope

of employment is “whether the agent is performing acts of the kind which he is authorized to perform, and those acts are motivated, at least in part, by an intent to benefit the corporation.”). In *United States v. Automated Medical Laboratories, Inc.*, 770 F.2d 399 (4th Cir. 1985), for example, the Fourth Circuit affirmed a corporation’s conviction for the actions of a subsidiary’s employee despite the corporation’s claim that the employee was acting for his own benefit, namely his “ambitious nature and his desire to ascend the corporate ladder.” *Id.* at 407. The court stated, “Partucci was clearly acting in part to benefit AML since his advancement within the corporation depended on AML’s well-being and its lack of difficulties with the FDA.” *Id.*; see also *United States v. Cincotta*, 689 F.2d 238, 241-42 (1st Cir. 1982) (upholding a corporation’s conviction, notwithstanding the substantial personal benefit reaped by its miscreant agents, because the fraudulent scheme required money to pass through the corporation’s treasury and the fraudulently obtained goods were resold to the corporation’s customers in the corporation’s name).

Moreover, the corporation need not even necessarily profit from its agent’s actions for it to be held liable. In *Automated Medical Laboratories*, the Fourth Circuit stated:

[B]enefit is not a “touchstone of criminal corporate liability; benefit at best is an evidential, not an operative, fact.” Thus, whether the agent’s actions ultimately redounded to the benefit of the corporation is less significant than whether the agent acted with the intent to benefit the corporation. The basic purpose of requiring that an agent have acted with the intent to benefit the corporation, however, is to insulate the corporation from criminal liability for actions of its agents which may be *inimical* to the interests of the corporation or which may have been undertaken solely to advance the interests of that agent or of a party other than the corporation.

770 F.2d at 407 (internal citation omitted) (quoting *Old Monastery Co. v. United States*, 147 F.2d 905, 908 (4th Cir. 1945)).

9-28.300 Factors to Be Considered

A. General Principle: Generally, prosecutors apply the same factors in determining whether to charge a corporation as they do with respect to individuals. See USAM § 9-27.220, *et seq.* Thus, the prosecutor must weigh all of the factors normally considered in the sound exercise of prosecutorial judgment: the sufficiency of the evidence; the likelihood of success at trial; the probable deterrent, rehabilitative, and other consequences of conviction; and the adequacy of noncriminal approaches. See *id.* However, due to the nature of the corporate “person,” some additional factors are present. In conducting an investigation, determining whether to bring charges, and negotiating plea or other agreements, prosecutors should consider the following factors in reaching a decision as to the proper treatment of a corporate target:

1. the nature and seriousness of the offense, including the risk of harm to the public, and applicable policies and priorities, if any, governing the prosecution of

- corporations for particular categories of crime (*see infra* section IV);
2. the pervasiveness of wrongdoing within the corporation, including the complicity in, or the condoning of, the wrongdoing by corporate management (*see infra* section V);
 3. the corporation's history of similar misconduct, including prior criminal, civil, and regulatory enforcement actions against it (*see infra* section VI);
 4. the corporation's timely and voluntary disclosure of wrongdoing and its willingness to cooperate in the investigation of its agents (*see infra* section VII);
 5. the existence and effectiveness of the corporation's pre-existing compliance program (*see infra* section VIII);
 6. the corporation's remedial actions, including any efforts to implement an effective corporate compliance program or to improve an existing one, to replace responsible management, to discipline or terminate wrongdoers, to pay restitution, and to cooperate with the relevant government agencies (*see infra* section IX);
 7. collateral consequences, including whether there is disproportionate harm to shareholders, pension holders, employees, and others not proven personally culpable, as well as impact on the public arising from the prosecution (*see infra* section X);
 8. the adequacy of the prosecution of individuals responsible for the corporation's malfeasance; and
 9. the adequacy of remedies such as civil or regulatory enforcement actions (*see infra* section XI).

B. Comment: The factors listed in this section are intended to be illustrative of those that should be evaluated and are not an exhaustive list of potentially relevant considerations. Some of these factors may not apply to specific cases, and in some cases one factor may override all others. For example, the nature and seriousness of the offense may be such as to warrant prosecution regardless of the other factors. In most cases, however, no single factor will be dispositive. In addition, national law enforcement policies in various enforcement areas may require that more or less weight be given to certain of these factors than to others. Of course, prosecutors must exercise their thoughtful and pragmatic judgment in applying and balancing these factors, so as to achieve a fair and just outcome and promote respect for the law.

In making a decision to charge a corporation, the prosecutor generally has substantial latitude in determining when, whom, how, and even whether to prosecute for violations of federal criminal law. In exercising that discretion, prosecutors should consider the following

statements of principles that summarize the considerations they should weigh and the practices they should follow in discharging their prosecutorial responsibilities. In doing so, prosecutors should ensure that the general purposes of the criminal law—assurance of warranted punishment, deterrence of further criminal conduct, protection of the public from dangerous and fraudulent conduct, rehabilitation of offenders, and restitution for victims and affected communities—are adequately met, taking into account the special nature of the corporate “person.”

9-28.400 Special Policy Concerns

A. General Principle: The nature and seriousness of the crime, including the risk of harm to the public from the criminal misconduct, are obviously primary factors in determining whether to charge a corporation. In addition, corporate conduct, particularly that of national and multi-national corporations, necessarily intersects with federal economic, tax, and criminal law enforcement policies. In applying these Principles, prosecutors must consider the practices and policies of the appropriate Division of the Department, and must comply with those policies to the extent required by the facts presented.

B. Comment: In determining whether to charge a corporation, prosecutors should take into account federal law enforcement priorities as discussed above. *See* USAM § 9-27-230. In addition, however, prosecutors must be aware of the specific policy goals and incentive programs established by the respective Divisions and regulatory agencies. Thus, whereas natural persons may be given incremental degrees of credit (ranging from immunity to lesser charges to sentencing considerations) for turning themselves in, making statements against their penal interest, and cooperating in the government’s investigation of their own and others’ wrongdoing, the same approach may not be appropriate in all circumstances with respect to corporations. As an example, it is entirely proper in many investigations for a prosecutor to consider the corporation’s pre-indictment conduct, e.g., voluntary disclosure, cooperation, remediation or restitution, in determining whether to seek an indictment. However, this would not necessarily be appropriate in an antitrust investigation, in which antitrust violations, by definition, go to the heart of the corporation’s business. With this in mind, the Antitrust Division has established a firm policy, understood in the business community, that credit should not be given at the charging stage for a compliance program and that amnesty is available only to the first corporation to make full disclosure to the government. As another example, the Tax Division has a strong preference for prosecuting responsible individuals, rather than entities, for corporate tax offenses. Thus, in determining whether or not to charge a corporation, prosecutors must consult with the Criminal, Antitrust, Tax, Environmental and Natural Resources, and National Security Divisions, as appropriate.

9-28.500 Pervasiveness of Wrongdoing Within the Corporation

A. General Principle: A corporation can only act through natural persons, and it is therefore held responsible for the acts of such persons fairly attributable to it. Charging a corporation for even minor misconduct may be appropriate where the wrongdoing was pervasive

and was undertaken by a large number of employees, or by all the employees in a particular role within the corporation, or was condoned by upper management. On the other hand, it may not be appropriate to impose liability upon a corporation, particularly one with a robust compliance program in place, under a strict *respondeat superior* theory for the single isolated act of a rogue employee. There is, of course, a wide spectrum between these two extremes, and a prosecutor should exercise sound discretion in evaluating the pervasiveness of wrongdoing within a corporation.

B. Comment: Of these factors, the most important is the role and conduct of management. Although acts of even low-level employees may result in criminal liability, a corporation is directed by its management and management is responsible for a corporate culture in which criminal conduct is either discouraged or tacitly encouraged. As stated in commentary to the Sentencing Guidelines:

Pervasiveness [is] case specific and [will] depend on the number, and degree of responsibility, of individuals [with] substantial authority . . . who participated in, condoned, or were willfully ignorant of the offense. Fewer individuals need to be involved for a finding of pervasiveness if those individuals exercised a relatively high degree of authority. Pervasiveness can occur either within an organization as a whole or within a unit of an organization.

USSG § 8C2.5, cmt. (n. 4).

9-28.600 The Corporation's Past History

A. General Principle: Prosecutors may consider a corporation's history of similar conduct, including prior criminal, civil, and regulatory enforcement actions against it, in determining whether to bring criminal charges and how best to resolve cases.

B. Comment: A corporation, like a natural person, is expected to learn from its mistakes. A history of similar misconduct may be probative of a corporate culture that encouraged, or at least condoned, such misdeeds, regardless of any compliance programs. Criminal prosecution of a corporation may be particularly appropriate where the corporation previously had been subject to non-criminal guidance, warnings, or sanctions, or previous criminal charges, and it either had not taken adequate action to prevent future unlawful conduct or had continued to engage in the misconduct in spite of the warnings or enforcement actions taken against it. The corporate structure itself (e.g., the creation or existence of subsidiaries or operating divisions) is not dispositive in this analysis, and enforcement actions taken against the corporation or any of its divisions, subsidiaries, and affiliates may be considered, if germane. See USSG § 8C2.5(c), cmt. (n. 6).

9-28.700 The Value of Cooperation

A. General Principle: In determining whether to charge a corporation and how to resolve corporate criminal cases, the corporation's timely and voluntary disclosure of wrongdoing and its cooperation with the government's investigation may be relevant factors. In 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.

Cooperation is a potential mitigating factor, by which a corporation—just like any other subject of a criminal investigation—can gain credit in a case that otherwise is appropriate for indictment and prosecution. Of course, the decision not to cooperate by a corporation (or individual) is not itself evidence of misconduct, at least where the lack of cooperation does not involve criminal misconduct or demonstrate consciousness of guilt (*e.g.*, suborning perjury or false statements, or refusing to comply with lawful discovery requests). Thus, failure to cooperate, in and of itself, does not support or require the filing of charges with respect to a corporation any more than with respect to an individual.

B. Comment: In investigating wrongdoing by or within a corporation, a prosecutor is likely to encounter several obstacles resulting from the nature of the corporation itself. It will often be difficult to determine which individual took which action on behalf of the corporation. Lines of authority and responsibility may be shared among operating divisions or departments, and records and personnel may be spread throughout the United States or even among several countries. Where the criminal conduct continued over an extended period of time, the culpable or knowledgeable personnel may have been promoted, transferred, or fired, or they may have quit or retired. Accordingly, a corporation's cooperation may be critical in identifying potentially relevant actors and locating relevant evidence, among other things, and in doing so expeditiously.

This dynamic—*i.e.*, the difficulty of determining what happened, where the evidence is, and which individuals took or promoted putatively illegal corporate actions—can have negative consequences for both the government and the corporation that is the subject or target of a government investigation. More specifically, because of corporate attribution principles concerning actions of corporate officers and employees (*see, e.g., supra* section II), uncertainty about exactly who authorized or directed apparent corporate misconduct can inure to the detriment of a corporation. For example, it may not matter under the law which of several possible executives or leaders in a chain of command approved of or authorized criminal conduct; however, that information if known might bear on the propriety of a particular disposition short of indictment of the corporation. It may not be in the interest of a corporation or the government for a charging decision to be made in the absence of such information, which might occur if, for example, a statute of limitations were relevant and authorization by any one of the officials were enough to justify a charge under the law. Moreover, and at a minimum, a

protracted government investigation of such an issue could, as a collateral consequence, disrupt the corporation's business operations or even depress its stock price.

For these reasons and more, cooperation can be a favorable course for both the government and the corporation. Cooperation benefits the government—and ultimately shareholders, employees, and other often blameless victims—by allowing prosecutors and federal agents, for example, to avoid protracted delays, which compromise their ability to quickly uncover and address the full extent of widespread corporate crimes. With cooperation by the corporation, the government may be able to reduce tangible losses, limit damage to reputation, and preserve assets for restitution. At the same time, cooperation may benefit the corporation by enabling the government to focus its investigative resources in a manner that will not unduly disrupt the corporation's legitimate business operations. In addition, and critically, cooperation may benefit the corporation by presenting it with the opportunity to earn credit for its efforts.

9-28.710 Attorney-Client and Work Product Protections

The attorney-client privilege and the attorney work product protection serve an extremely important function in the American legal system. The attorney-client privilege is one of the oldest and most sacrosanct privileges under the law. See *Upjohn v. United States*, 449 U.S. 383, 389 (1981). As the Supreme Court has stated, “[i]ts purpose is to encourage full and frank communication between attorneys and their clients and thereby promote broader public interests in the observance of law and administration of justice.” *Id.* The value of promoting a corporation's ability to seek frank and comprehensive legal advice is particularly important in the contemporary global business environment, where corporations often face complex and dynamic legal and regulatory obligations imposed by the federal government and also by states and foreign governments. The work product doctrine serves similarly important goals.

For these reasons, waiving the attorney-client and work product protections has never been a prerequisite under the Department's prosecution guidelines for a corporation to be viewed as cooperative. Nonetheless, a wide range of commentators and members of the American legal community and criminal justice system have asserted that the Department's policies have been used, either wittingly or unwittingly, to coerce business entities into waiving attorney-client privilege and work-product protection. Everyone agrees that a corporation may freely waive its own privileges if it chooses to do so; indeed, such waivers occur routinely when corporations are victimized by their employees or others, conduct an internal investigation, and then disclose the details of the investigation to law enforcement officials in an effort to seek prosecution of the offenders. However, the contention, from a broad array of voices, is that the Department's position on attorney-client privilege and work product protection waivers has promoted an environment in which those protections are being unfairly eroded to the detriment of all.

The Department understands that the attorney-client privilege and attorney work product protection are essential and long-recognized components of the American legal system. 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. In addition, while a corporation remains free to convey non-factual or “core” attorney-client communications or work product—if and only if the corporation voluntarily chooses to do so—prosecutors should not ask for such waivers and are directed not to do so. The critical factor is whether the corporation has provided the facts about the events, as explained further herein.

9-28.720 Cooperation: Disclosing the Relevant Facts

Eligibility for cooperation credit is not predicated upon the waiver of attorney-client privilege or work product protection. Instead, the sort of cooperation that is most valuable to resolving allegations of misconduct by a corporation and its officers, directors, employees, or agents is disclosure of the relevant *facts* concerning such misconduct. In this regard, the analysis parallels that for a non-corporate defendant, where cooperation typically requires disclosure of relevant factual knowledge and not of discussions between an individual and his attorneys.

Thus, when the government investigates potential corporate wrongdoing, it seeks the relevant facts. For example, how and when did the alleged misconduct occur? Who promoted or approved it? Who was responsible for committing it? In this respect, the investigation of a corporation differs little from the investigation of an individual. In both cases, the government needs to know the facts to achieve a just and fair outcome. The party under investigation may choose to cooperate by disclosing the facts, and the government may give credit for the party’s disclosures. If a corporation wishes to receive credit for such cooperation, which then can be considered with all other cooperative efforts and circumstances in evaluating how fairly to proceed, then the corporation, like any person, must disclose the relevant facts of which it has knowledge.²

(a) Disclosing the Relevant Facts – Facts Gathered Through Internal Investigation

Individuals and corporations often obtain knowledge of facts in different ways. An individual knows the facts of his or others’ misconduct through his own experience and perceptions. A corporation is an artificial construct that cannot, by definition, have personal knowledge of the facts. Some of those facts may be reflected in documentary or electronic media like emails, transaction or accounting documents, and other records. Often, the corporation gathers facts through an internal investigation. Exactly how and by whom the facts

² There are other dimensions of cooperation beyond the mere disclosure of facts, of course. These can include, for example, providing non-privileged documents and other evidence, making witnesses available for interviews, and assisting in the interpretation of complex business records. This section of the Principles focuses solely on the disclosure of facts and the privilege issues that may be implicated thereby.

are gathered is for the corporation to decide. Many corporations choose to collect information about potential misconduct through lawyers, a process that may confer attorney-client privilege or attorney work product protection on at least some of the information collected. Other corporations may choose a method of fact-gathering that does not have that effect—for example, having employee or other witness statements collected after interviews by non-attorney personnel.

Whichever process the corporation selects, the government's key measure of cooperation must remain the same as it does for an individual: has the party timely disclosed the relevant facts about the putative misconduct? That is the operative question in assigning cooperation credit for the disclosure of information—not whether the corporation discloses attorney-client or work product materials. Accordingly, a corporation should receive the same credit for disclosing facts contained in materials that are not protected by the attorney-client privilege or attorney work product as it would for disclosing identical facts contained in materials that are so protected.³ On this point the Report of the House Judiciary Committee, submitted in connection with the attorney-client privilege bill passed by the House of Representatives (H.R. 3013), comports with the approach required here:

[A]n . . . attorney of the United States may base cooperation credit on the facts that are disclosed, but is prohibited from basing cooperation credit upon whether or not the materials are protected by attorney-client privilege or attorney work product. As a result, an entity that voluntarily discloses should receive the same amount of cooperation credit for disclosing facts that happen to be contained in materials not protected by attorney-client privilege or attorney work product as it would receive for disclosing identical facts that are contained in materials protected by attorney-client privilege or attorney work product. There should be no differentials in an assessment of cooperation (i.e., neither a credit nor a penalty) based upon whether or not the materials disclosed are protected by attorney-client privilege or attorney work product.

H.R. Rep. No. 110-445 at 4 (2007).

³ By way of example, corporate personnel are typically interviewed during an internal investigation. If the interviews are conducted by counsel for the corporation, certain notes and memoranda generated from the interviews may be subject, at least in part, to the protections of attorney-client privilege and/or attorney work product. To receive cooperation credit for providing factual information, the corporation need not produce, and prosecutors may not request, protected notes or memoranda generated by the lawyers' interviews. To earn such credit, however, the corporation does need to produce, and prosecutors may request, relevant factual information—including relevant factual information acquired through those interviews, unless the identical information has otherwise been provided—as well as relevant non-privileged evidence such as accounting and business records and emails between non-attorney employees or agents.

In short, so long as the corporation timely discloses relevant facts about the putative misconduct, the corporation may receive due credit for such cooperation, regardless of whether it chooses to waive privilege or work product protection in the process.⁴ Likewise, a corporation that does not disclose the relevant facts about the alleged misconduct—for whatever reason—typically should not be entitled to receive credit for cooperation.

Two final and related points bear noting about the disclosure of facts, although they should be obvious. First, the government cannot compel, and the corporation has no obligation to make, such disclosures (although the government can obviously compel the disclosure of certain records and witness testimony through subpoenas). Second, a corporation's failure to provide relevant information does not mean the corporation will be indicted. It simply means that the corporation will not be entitled to mitigating credit for that cooperation. Whether the corporation faces charges will turn, as it does in any case, on the sufficiency of the evidence, the likelihood of success at trial, and all of the other factors identified in Section III above. If there is insufficient evidence to warrant indictment, after appropriate investigation has been completed, or if the other factors weigh against indictment, then the corporation should not be indicted, irrespective of whether it has earned cooperation credit. The converse is also true: The government may charge even the most cooperative corporation pursuant to these Principles if, in weighing and balancing the factors described herein, the prosecutor determines that a charge is required in the interests of justice. Put differently, even the most sincere and thorough effort to cooperate cannot necessarily absolve a corporation that has, for example, engaged in an egregious, orchestrated, and widespread fraud. Cooperation is a relevant potential mitigating factor, but it alone is not dispositive.

(b) Legal Advice and Attorney Work Product

Separate from (and usually preceding) the fact-gathering process in an internal investigation, a corporation, through its officers, employees, directors, or others, may have consulted with corporate counsel regarding or in a manner that concerns the legal implications of the putative misconduct at issue. Communications of this sort, which are both independent of the fact-gathering component of an internal investigation and made for the purpose of seeking or dispensing legal advice, lie at the core of the attorney-client privilege. Such communications can naturally have a salutary effect on corporate behavior—facilitating, for example, a corporation's effort to comply with complex and evolving legal and regulatory regimes.⁵ Except as noted in

⁴ In assessing the timeliness of a corporation's disclosures, prosecutors should apply a standard of reasonableness in light of the totality of circumstances.

⁵ These privileged communications are not necessarily limited to those that occur contemporaneously with the underlying misconduct. They would include, for instance, legal advice provided by corporate counsel in an internal investigation report. Again, the key measure of cooperation is the disclosure of factual information known to the corporation, not the

subparagraphs (b)(i) and (b)(ii) below, a corporation need not disclose and prosecutors may not request the disclosure of such communications as a condition for the corporation's eligibility to receive cooperation credit.

Likewise, non-factual or core attorney work product—for example, an attorney's mental impressions or legal theories—lies at the core of the attorney work product doctrine. A corporation need not disclose, and prosecutors may not request, the disclosure of such attorney work product as a condition for the corporation's eligibility to receive cooperation credit.

(i) Advice of Counsel Defense in the Instant Context

Occasionally a corporation or one of its employees may assert an advice-of-counsel defense, based upon communications with in-house or outside counsel that took place prior to or contemporaneously with the underlying conduct at issue. In such situations, the defendant must tender a legitimate factual basis to support the assertion of the advice-of-counsel defense. *See, e.g., Pitt v. Dist. of Columbia*, 491 F.3d 494, 504-05 (D.C. Cir. 2007); *United States v. Wenger*, 427 F.3d 840, 853-54 (10th Cir. 2005); *United States v. Cheek*, 3 F.3d 1057, 1061-62 (7th Cir. 1993). The Department cannot fairly be asked to discharge its responsibility to the public to investigate alleged corporate crime, or to temper what would otherwise be the appropriate course of prosecutive action, by simply accepting on faith an otherwise unproven assertion that an attorney—perhaps even an unnamed attorney—approved potentially unlawful practices. Accordingly, where an advice-of-counsel defense has been asserted, prosecutors may ask for the disclosure of the communications allegedly supporting it.

(ii) Communications in Furtherance of a Crime or Fraud

Communications between a corporation (through its officers, employees, directors, or agents) and corporate counsel that are made in furtherance of a crime or fraud are, under settled precedent, outside the scope and protection of the attorney-client privilege. *See United States v. Zolin*, 491 U.S. 554, 563 (1989); *United States v. BDO Seidman, LLP*, 492 F.3d 806, 818 (7th Cir. 2007). As a result, the Department may properly request such communications if they in fact exist.

9-28.730 Obstructing the Investigation

Another factor to be weighed by the prosecutor is whether the corporation has engaged in conduct intended to impede the investigation. Examples of such conduct could include: inappropriate directions to employees or their counsel, such as directions not to be truthful or to conceal relevant facts; making representations or submissions that contain misleading assertions or material omissions; and incomplete or delayed production of records.

disclosure of legal advice or theories rendered in connection with the conduct at issue (subject to the two exceptions noted in Section VII(2)(b)(i-ii)).

In evaluating cooperation, however, prosecutors should not take into account whether a corporation is advancing or reimbursing attorneys' fees or providing counsel to employees, officers, or directors under investigation or indictment. Likewise, prosecutors may not request that a corporation refrain from taking such action. This prohibition is not meant to prevent a prosecutor from asking questions about an attorney's representation of a corporation or its employees, officers, or directors, where otherwise appropriate under the law.⁶ Neither is it intended to limit the otherwise applicable reach of criminal obstruction of justice statutes such as 18 U.S.C. § 1503. If the payment of attorney fees were used in a manner that would otherwise constitute criminal obstruction of justice—for example, if fees were advanced on the condition that an employee adhere to a version of the facts that the corporation and the employee knew to be false—these Principles would not (and could not) render inapplicable such criminal prohibitions.

Similarly, the mere participation by a corporation in a joint defense agreement does not render the corporation ineligible to receive cooperation credit, and prosecutors may not request that a corporation refrain from entering into such agreements. Of course, the corporation may wish to avoid putting itself in the position of being disabled, by virtue of a particular joint defense or similar agreement, from providing some relevant facts to the government and thereby limiting its ability to seek such cooperation credit. Such might be the case if the corporation gathers facts from employees who have entered into a joint defense agreement with the corporation, and who may later seek to prevent the corporation from disclosing the facts it has acquired. Corporations may wish to address this situation by crafting or participating in joint defense agreements, to the extent they choose to enter them, that provide such flexibility as they deem appropriate.

Finally, it may on occasion be appropriate for the government to consider whether the corporation has shared with others sensitive information about the investigation that the government provided to the corporation. In appropriate situations, as it does with individuals, the government may properly request that, if a corporation wishes to receive credit for cooperation, the information provided by the government to the corporation not be transmitted to others—for example, where the disclosure of such information could lead to flight by individual subjects, destruction of evidence, or dissipation or concealment of assets.

9-28.740 Offering Cooperation: No Entitlement to Immunity

A corporation's offer of cooperation or cooperation itself does not automatically entitle it to immunity from prosecution or a favorable resolution of its case. A corporation should not be able to escape liability merely by offering up its directors, officers, employees, or agents. Thus,

⁶ Routine questions regarding the representation status of a corporation and its employees, including how and by whom attorneys' fees are paid, sometimes arise in the course of an investigation under certain circumstances—to take one example, to assess conflict-of-interest issues. Such questions can be appropriate and this guidance is not intended to prohibit such limited inquiries.

a corporation's willingness to cooperate is not determinative; that factor, while relevant, needs to be considered in conjunction with all other factors.

9-28.750 **Qualifying for Immunity, Amnesty, or Reduced Sanctions Through Voluntary Disclosures**

In conjunction with regulatory agencies and other executive branch departments, the Department encourages corporations, as part of their compliance programs, to conduct internal investigations and to disclose the relevant facts to the appropriate authorities. Some agencies, such as the Securities and Exchange Commission and the Environmental Protection Agency, as well as the Department's Environmental and Natural Resources Division, have formal voluntary disclosure programs in which self-reporting, coupled with remediation and additional criteria, may qualify the corporation for amnesty or reduced sanctions. Even in the absence of a formal program, prosecutors may consider a corporation's timely and voluntary disclosure in evaluating the adequacy of the corporation's compliance program and its management's commitment to the compliance program. However, prosecution and economic policies specific to the industry or statute may require prosecution notwithstanding a corporation's willingness to cooperate. For example, the Antitrust Division has a policy of offering amnesty only to the first corporation to agree to cooperate. Moreover, amnesty, immunity, or reduced sanctions may not be appropriate where the corporation's business is permeated with fraud or other crimes.

9-28.760 **Oversight Concerning Demands for Waivers of Attorney-Client Privilege or Work Product Protection By Corporations Contrary to This Policy**

The Department underscores its commitment to attorney practices that are consistent with Department policies like those set forth herein concerning cooperation credit and due respect for the attorney-client privilege and work product protection. Counsel for corporations who believe that prosecutors are violating such guidance are encouraged to raise their concerns with supervisors, including the appropriate United States Attorney or Assistant Attorney General. Like any other allegation of attorney misconduct, such allegations are subject to potential investigation through established mechanisms.

9-28.800 **Corporate Compliance Programs**

A. **General Principle:** Compliance programs are established by corporate management to prevent and detect misconduct and to ensure that corporate activities are conducted in accordance with applicable criminal and civil laws, regulations, and rules. The Department encourages such corporate self-policing, including voluntary disclosures to the government of any problems that a corporation discovers on its own. However, the existence of a compliance program is not sufficient, in and of itself, to justify not charging a corporation for criminal misconduct undertaken by its officers, directors, employees, or agents. In addition, the nature of some crimes, e.g., antitrust violations, may be such that national law enforcement policies mandate prosecutions of corporations notwithstanding the existence of a compliance program.

B. Comment: The existence of a corporate compliance program, even one that specifically prohibited the very conduct in question, does not absolve the corporation from criminal liability under the doctrine of *respondet superior*. See *United States v. Basic Constr. Co.*, 711 F.2d 570, 573 (4th Cir. 1983) (“[A] corporation may be held criminally responsible for antitrust violations committed by its employees if they were acting within the scope of their authority, or apparent authority, and for the benefit of the corporation, even if . . . such acts were against corporate policy or express instructions.”). As explained in *United States v. Potter*, 463 F.3d 9 (1st Cir. 2006), a corporation cannot “avoid liability by adopting abstract rules” that forbid its agents from engaging in illegal acts, because “[e]ven a specific directive to an agent or employee or honest efforts to police such rules do not automatically free the company for the wrongful acts of agents.” *Id.* at 25-26. See also *United States v. Hilton Hotels Corp.*, 467 F.2d 1000, 1007 (9th Cir. 1972) (noting that a corporation “could not gain exculpation by issuing general instructions without undertaking to enforce those instructions by means commensurate with the obvious risks”); *United States v. Beusch*, 596 F.2d 871, 878 (9th Cir. 1979) (“[A] corporation may be liable for acts of its employees done contrary to express instructions and policies, but . . . the existence of such instructions and policies may be considered in determining whether the employee in fact acted to benefit the corporation.”).

While the Department recognizes that no compliance program can ever prevent all criminal activity by a corporation’s employees, the critical factors in evaluating any program are whether the program is adequately designed for maximum effectiveness in preventing and detecting wrongdoing by employees and whether corporate management is enforcing the program or is tacitly encouraging or pressuring employees to engage in misconduct to achieve business objectives. The Department has no formulaic requirements regarding corporate compliance programs. The fundamental questions any prosecutor should ask are: Is the corporation’s compliance program well designed? Is the program being applied earnestly and in good faith? Does the corporation’s compliance program work? In answering these questions, the prosecutor should consider the comprehensiveness of the compliance program; the extent and pervasiveness of the criminal misconduct; the number and level of the corporate employees involved; the seriousness, duration, and frequency of the misconduct; and any remedial actions taken by the corporation, including, for example, disciplinary action against past violators uncovered by the prior compliance program, and revisions to corporate compliance programs in light of lessons learned.⁷ Prosecutors should also consider the promptness of any disclosure of wrongdoing to the government. In evaluating compliance programs, prosecutors may consider whether the corporation has established corporate governance mechanisms that can effectively detect and prevent misconduct. For example, do the corporation’s directors exercise independent review over proposed corporate actions rather than unquestioningly ratifying officers’ recommendations; are internal audit functions conducted at a level sufficient to ensure their independence and accuracy; and have the directors established an information and reporting system in the organization reasonably designed to provide management and directors with timely and accurate information sufficient to allow them to reach an informed decision regarding the

⁷ For a detailed review of these and other factors concerning corporate compliance programs, see USSG § 8B2.1.

organization's compliance with the law. *See, e.g., In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959, 968-70 (Del. Ch. 1996).

Prosecutors should therefore attempt to determine whether a corporation's compliance program is merely a "paper program" or whether it was designed, implemented, reviewed, and revised, as appropriate, in an effective manner. In addition, prosecutors should determine whether the corporation has provided for a staff sufficient to audit, document, analyze, and utilize the results of the corporation's compliance efforts. Prosecutors also should determine whether the corporation's employees are adequately informed about the compliance program and are convinced of the corporation's commitment to it. This will enable the prosecutor to make an informed decision as to whether the corporation has adopted and implemented a truly effective compliance program that, when consistent with other federal law enforcement policies, may result in a decision to charge only the corporation's employees and agents or to mitigate charges or sanctions against the corporation.

Compliance programs should be designed to detect the particular types of misconduct most likely to occur in a particular corporation's line of business. Many corporations operate in complex regulatory environments outside the normal experience of criminal prosecutors. Accordingly, prosecutors should consult with relevant federal and state agencies with the expertise to evaluate the adequacy of a program's design and implementation. For instance, state and federal banking, insurance, and medical boards, the Department of Defense, the Department of Health and Human Services, the Environmental Protection Agency, and the Securities and Exchange Commission have considerable experience with compliance programs and can be helpful to a prosecutor in evaluating such programs. In addition, the Fraud Section of the Criminal Division, the Commercial Litigation Branch of the Civil Division, and the Environmental Crimes Section of the Environment and Natural Resources Division can assist United States Attorneys' Offices in finding the appropriate agency office(s) for such consultation.

9-28.900 Restitution and Remediation

A. General Principle: Although neither a corporation nor an individual target may avoid prosecution merely by paying a sum of money, a prosecutor may consider the corporation's willingness to make restitution and steps already taken to do so. A prosecutor may also consider other remedial actions, such as improving an existing compliance program or disciplining wrongdoers, in determining whether to charge the corporation and how to resolve corporate criminal cases.

B. Comment: In determining whether or not to prosecute a corporation, the government may consider whether the corporation has taken meaningful remedial measures. A corporation's response to misconduct says much about its willingness to ensure that such misconduct does not recur. Thus, corporations that fully recognize the seriousness of their misconduct and accept responsibility for it should be taking steps to implement the personnel, operational, and

organizational changes necessary to establish an awareness among employees that criminal conduct will not be tolerated.

Among the factors prosecutors should consider and weigh are whether the corporation appropriately disciplined wrongdoers, once those employees are identified by the corporation as culpable for the misconduct. Employee discipline is a difficult task for many corporations because of the human element involved and sometimes because of the seniority of the employees concerned. Although corporations need to be fair to their employees, they must also be committed, at all levels of the corporation, to the highest standards of legal and ethical behavior. Effective internal discipline can be a powerful deterrent against improper behavior by a corporation's employees. Prosecutors should be satisfied that the corporation's focus is on the integrity and credibility of its remedial and disciplinary measures rather than on the protection of the wrongdoers.

In addition to employee discipline, two other factors used in evaluating a corporation's remedial efforts are restitution and reform. As with natural persons, the decision whether or not to prosecute should not depend upon the target's ability to pay restitution. A corporation's efforts to pay restitution even in advance of any court order is, however, evidence of its acceptance of responsibility and, consistent with the practices and policies of the appropriate Division of the Department entrusted with enforcing specific criminal laws, may be considered in determining whether to bring criminal charges. Similarly, although the inadequacy of a corporate compliance program is a factor to consider when deciding whether to charge a corporation, that corporation's quick recognition of the flaws in the program and its efforts to improve the program are also factors to consider as to appropriate disposition of a case.

9-28.1000 Collateral Consequences

A. General Principle: Prosecutors may consider the collateral consequences of a corporate criminal conviction or indictment in determining whether to charge the corporation with a criminal offense and how to resolve corporate criminal cases.

B. Comment: One of the factors in determining whether to charge a natural person or a corporation is whether the likely punishment is appropriate given the nature and seriousness of the crime. In the corporate context, prosecutors may take into account the possibly substantial consequences to a corporation's employees, investors, pensioners, and customers, many of whom may, depending on the size and nature of the corporation and their role in its operations, have played no role in the criminal conduct, have been unaware of it, or have been unable to prevent it. Prosecutors should also be aware of non-penal sanctions that may accompany a criminal charge, such as potential suspension or debarment from eligibility for government contracts or federally funded programs such as health care programs. Determining whether or not such non-penal sanctions are appropriate or required in a particular case is the responsibility of the relevant agency, and is a decision that will be made based on the applicable statutes, regulations, and policies.

Virtually every conviction of a corporation, like virtually every conviction of an individual, will have an impact on innocent third parties, and the mere existence of such an effect is not sufficient to preclude prosecution of the corporation. Therefore, in evaluating the relevance of collateral consequences, various factors already discussed, such as the pervasiveness of the criminal conduct and the adequacy of the corporation's compliance programs, should be considered in determining the weight to be given to this factor. For instance, the balance may tip in favor of prosecuting corporations in situations where the scope of the misconduct in a case is widespread and sustained within a corporate division (or spread throughout pockets of the corporate organization). In such cases, the possible unfairness of visiting punishment for the corporation's crimes upon shareholders may be of much less concern where those shareholders have substantially profited, even unknowingly, from widespread or pervasive criminal activity. Similarly, where the top layers of the corporation's management or the shareholders of a closely-held corporation were engaged in or aware of the wrongdoing, and the conduct at issue was accepted as a way of doing business for an extended period, debarment may be deemed not collateral, but a direct and entirely appropriate consequence of the corporation's wrongdoing.

On the other hand, where the collateral consequences of a corporate conviction for innocent third parties would be significant, it may be appropriate to consider a non-prosecution or deferred prosecution agreement with conditions designed, among other things, to promote compliance with applicable law and to prevent recidivism. Such agreements are a third option, besides a criminal indictment, on the one hand, and a declination, on the other. Declining prosecution may allow a corporate criminal to escape without consequences. Obtaining a conviction may produce a result that seriously harms innocent third parties who played no role in the criminal conduct. Under appropriate circumstances, a deferred prosecution or non-prosecution agreement can help restore the integrity of a company's operations and preserve the financial viability of a corporation that has engaged in criminal conduct, while preserving the government's ability to prosecute a recalcitrant corporation that materially breaches the agreement. Such agreements achieve other important objectives as well, like prompt restitution for victims.⁸ Ultimately, the appropriateness of a criminal charge against a corporation, or some lesser alternative, must be evaluated in a pragmatic and reasoned way that produces a fair outcome, taking into consideration, among other things, the Department's need to promote and ensure respect for the law.

9-28.1100 Other Civil or Regulatory Alternatives

A. General Principle: Non-criminal alternatives to prosecution often exist and prosecutors may consider whether such sanctions would adequately deter, punish, and rehabilitate a corporation that has engaged in wrongful conduct. In evaluating the adequacy of

⁸ Prosecutors should note that in the case of national or multi-national corporations, multi-district or global agreements may be necessary. Such agreements may only be entered into with the approval of each affected district or the appropriate Department official. *See id.* § 9-27.641.

non-criminal alternatives to prosecution—e.g., civil or regulatory enforcement actions—the prosecutor may consider all relevant factors, including:

1. the sanctions available under the alternative means of disposition;
2. the likelihood that an effective sanction will be imposed; and
3. the effect of non-criminal disposition on federal law enforcement interests.

B. Comment: The primary goals of criminal law are deterrence, punishment, and rehabilitation. Non-criminal sanctions may not be an appropriate response to a serious violation, a pattern of wrongdoing, or prior non-criminal sanctions without proper remediation. In other cases, however, these goals may be satisfied through civil or regulatory actions. In determining whether a federal criminal resolution is appropriate, the prosecutor should consider the same factors (modified appropriately for the regulatory context) considered when determining whether to leave prosecution of a natural person to another jurisdiction or to seek non-criminal alternatives to prosecution. These factors include: the strength of the regulatory authority's interest; the regulatory authority's ability and willingness to take effective enforcement action; the probable sanction if the regulatory authority's enforcement action is upheld; and the effect of a non-criminal disposition on federal law enforcement interests. See USAM §§ 9-27.240, 9-27.250.

9-28.1200 Selecting Charges

A. General Principle: Once a prosecutor has decided to charge a corporation, the prosecutor at least presumptively should charge, or should recommend that the grand jury charge, the most serious offense that is consistent with the nature of the defendant's misconduct and that is likely to result in a sustainable conviction.

B. Comment: Once the decision to charge is made, the same rules as govern charging natural persons apply. These rules require "a faithful and honest application of the Sentencing Guidelines" and an "individualized assessment of the extent to which particular charges fit the specific circumstances of the case, are consistent with the purposes of the Federal criminal code, and maximize the impact of Federal resources on crime." See USAM § 9-27.300. In making this determination, "it is appropriate that the attorney for the government consider, *inter alia*, such factors as the [advisory] sentencing guideline range yielded by the charge, whether the penalty yielded by such sentencing range . . . is proportional to the seriousness of the defendant's conduct, and whether the charge achieves such purposes of the criminal law as punishment, protection of the public, specific and general deterrence, and rehabilitation." *Id.*

9-28.1300 Plea Agreements with Corporations

A. General Principle: In negotiating plea agreements with corporations, as with individuals, prosecutors should generally seek a plea to the most serious, readily provable

offense charged. In addition, the terms of the plea agreement should contain appropriate provisions to ensure punishment, deterrence, rehabilitation, and compliance with the plea agreement in the corporate context. Although special circumstances may mandate a different conclusion, prosecutors generally should not agree to accept a corporate guilty plea in exchange for non-prosecution or dismissal of charges against individual officers and employees.

B. Comment: Prosecutors may enter into plea agreements with corporations for the same reasons and under the same constraints as apply to plea agreements with natural persons. See USAM §§ 9-27.400-530. This means, *inter alia*, that the corporation should generally be required to plead guilty to the most serious, readily provable offense charged. In addition, any negotiated departures or recommended variances from the advisory Sentencing Guidelines must be justifiable under the Guidelines or 18 U.S.C. § 3553 and must be disclosed to the sentencing court. A corporation should be made to realize that pleading guilty to criminal charges constitutes an admission of guilt and not merely a resolution of an inconvenient distraction from its business. As with natural persons, pleas should be structured so that the corporation may not later "proclaim lack of culpability or even complete innocence." See USAM §§ 9-27.420(b)(4), 9-27.440, 9-27.500. Thus, for instance, there should be placed upon the record a sufficient factual basis for the plea to prevent later corporate assertions of innocence.

A corporate plea agreement should also contain provisions that recognize the nature of the corporate "person" and that ensure that the principles of punishment, deterrence, and rehabilitation are met. In the corporate context, punishment and deterrence are generally accomplished by substantial fines, mandatory restitution, and institution of appropriate compliance measures, including, if necessary, continued judicial oversight or the use of special masters or corporate monitors. See USSG §§ 8B1.1, 8C2.1, *et seq.* In addition, where the corporation is a government contractor, permanent or temporary debarment may be appropriate. Where the corporation was engaged in fraud against the government (*e.g.*, contracting fraud), a prosecutor may not negotiate away an agency's right to debar or delist the corporate defendant.

In negotiating a plea agreement, prosecutors should also consider the deterrent value of prosecutions of individuals within the corporation. Therefore, one factor that a prosecutor may consider in determining whether to enter into a plea agreement is whether the corporation is seeking immunity for its employees and officers or whether the corporation is willing to cooperate in the investigation of culpable individuals as outlined herein. Prosecutors should rarely negotiate away individual criminal liability in a corporate plea.

Rehabilitation, of course, requires that the corporation undertake to be law-abiding in the future. It is, therefore, appropriate to require the corporation, as a condition of probation, to implement a compliance program or to reform an existing one. As discussed above, prosecutors may consult with the appropriate state and federal agencies and components of the Justice Department to ensure that a proposed compliance program is adequate and meets industry standards and best practices. See *supra* section VIII.

In plea agreements in which the corporation agrees to cooperate, the prosecutor should ensure that the cooperation is entirely truthful. To do so, the prosecutor may request that the corporation make appropriate disclosures of relevant factual information and documents, make employees and agents available for debriefing, file appropriate certified financial statements, agree to governmental or third-party audits, and take whatever other steps are necessary to ensure that the full scope of the corporate wrongdoing is disclosed and that the responsible personnel are identified and, if appropriate, prosecuted. *See generally supra* section VII. In taking such steps, Department prosecutors should recognize that attorney-client communications are often essential to a corporation's efforts to comply with complex regulatory and legal regimes, and that, as discussed at length above, cooperation is not measured by the waiver of attorney-client privilege and work product protection, but rather is measured by the disclosure of facts and other considerations identified herein such as making witnesses available for interviews and assisting in the interpretation of complex documents or business records.

These Principles provide only internal Department of Justice guidance. They are not intended to, do not, and may not be relied upon to create any rights, substantive or procedural, enforceable at law by any party in any matter civil or criminal. Nor are any limitations hereby placed on otherwise lawful litigative prerogatives of the Department of Justice.

Appendix D



U.S. Securities and Exchange Commission

SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 44969 / October 23, 2001

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 1470 / October 23, 2001

Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934 and Commission Statement on the Relationship of Cooperation to Agency Enforcement Decisions

Today, we commence and settle a cease-and-desist proceeding against Gisela de Leon-Meredith, former controller of a public company's subsidiary.¹ Our order finds that Meredith caused the parent company's books and records to be inaccurate and its periodic reports misstated, and then covered up those facts.

We are not taking action against the parent company, given the nature of the conduct and the company's responses. Within a week of learning about the apparent misconduct, the company's internal auditors had conducted a preliminary review and had advised company management who, in turn, advised the Board's audit committee, that Meredith had caused the company's books and records to be inaccurate and its financial reports to be misstated. The full Board was advised and authorized the company to hire an outside law firm to conduct a thorough inquiry. Four days later, Meredith was dismissed, as were two other employees who, in the company's view, had inadequately supervised Meredith; a day later, the company disclosed publicly and to us that its financial statements would be restated. The price of the company's shares did not decline after the announcement or after the restatement was published. The company pledged and gave complete cooperation to our staff. It provided the staff with all information relevant to the underlying violations. Among other things, the company produced the details of its internal investigation, including notes and transcripts of interviews of Meredith and others; and it did not invoke the attorney-client privilege, work product protection or other privileges or protections with respect to any facts uncovered in the investigation.

The company also strengthened its financial reporting processes to address Meredith's conduct -- developing a detailed closing process for the subsidiary's accounting personnel, consolidating subsidiary accounting functions under a parent company CPA, hiring three new CPAs for the accounting department responsible for preparing the subsidiary's financial

Reports of Investigations:

statements, redesigning the subsidiary's minimum annual audit requirements, and requiring the parent company's controller to interview and approve all senior accounting personnel in its subsidiaries' reporting processes.

Our willingness to credit such behavior in deciding whether and how to take enforcement action benefits investors as well as our enforcement program. When businesses seek out, self-report and rectify illegal conduct, and otherwise cooperate with Commission staff, large expenditures of government and shareholder resources can be avoided and investors can benefit more promptly.² In setting forth the criteria listed below, we think a few caveats are in order:

First, the paramount issue in every enforcement judgment is, and must be, what best protects investors. There is no single, or constant, answer to that question. Self-policing, self-reporting, remediation and cooperation with law enforcement authorities, among other things, are unquestionably important in promoting investors' best interests. But, so too are vigorous enforcement and the imposition of appropriate sanctions where the law has been violated. Indeed, there may be circumstances where conduct is so egregious, and harm so great, that no amount of cooperation or other mitigating conduct can justify a decision not to bring any enforcement action at all. In the end, no set of criteria can, or should, be strictly applied in every situation to which they may be applicable.

Second, we are not adopting any rule or making any commitment or promise about any specific case; nor are we in any way limiting our broad discretion to evaluate every case individually, on its own particular facts and circumstances. Conversely, we are not conferring any "rights" on any person or entity. We seek only to convey an understanding of the factors that may influence our decisions.

Third, we do not limit ourselves to the criteria we discuss below. By definition, enforcement judgments are just that -- judgments. Our failure to mention a specific criterion in one context does not preclude us from relying on that criterion in another. Further, the fact that a company has satisfied all the criteria we list below will not foreclose us from bringing enforcement proceedings that we believe are necessary or appropriate, for the benefit of investors.

In brief form, we set forth below some of the criteria we will consider in determining whether, and how much, to credit self-policing, self-reporting, remediation and cooperation -- from the extraordinary step of taking no enforcement action to bringing reduced charges, seeking lighter sanctions, or including mitigating language in documents we use to announce and resolve enforcement actions.

1. What is the nature of the misconduct involved? Did it result from inadvertence, honest mistake, simple negligence, reckless or deliberate indifference to indicia of wrongful conduct, willful misconduct or unadorned

venality? Were the company's auditors misled?

2. How did the misconduct arise? Is it the result of pressure placed on employees to achieve specific results, or a tone of lawlessness set by those in control of the company? What compliance procedures were in place to prevent the misconduct now uncovered? Why did those procedures fail to stop or inhibit the wrongful conduct?

3. Where in the organization did the misconduct occur? How high up in the chain of command was knowledge of, or participation in, the misconduct? Did senior personnel participate in, or turn a blind eye toward, obvious indicia of misconduct? How systemic was the behavior? Is it symptomatic of the way the entity does business, or was it isolated?

4. How long did the misconduct last? Was it a one-quarter, or one-time, event, or did it last several years? In the case of a public company, did the misconduct occur before the company went public? Did it facilitate the company's ability to go public?

5. How much harm has the misconduct inflicted upon investors and other corporate constituencies? Did the share price of the company's stock drop significantly upon its discovery and disclosure?

6. How was the misconduct detected and who uncovered it?

7. How long after discovery of the misconduct did it take to implement an effective response?

8. What steps did the company take upon learning of the misconduct? Did the company immediately stop the misconduct? Are persons responsible for any misconduct still with the company? If so, are they still in the same positions? Did the company promptly, completely and effectively disclose the existence of the misconduct to the public, to regulators and to self-regulators? Did the company cooperate completely with appropriate regulatory and law enforcement bodies? Did the company identify what additional related misconduct is likely to have occurred? Did the company take steps to identify the extent of damage to investors and other corporate constituencies? Did the company appropriately recompense those adversely affected by the conduct?

9. What processes did the company follow to resolve many of these issues and ferret out necessary information? Were the Audit Committee and the Board of Directors fully informed? If so, when?

10. Did the company commit to learn the truth, fully and expeditiously? Did it do a thorough review of the nature, extent, origins and consequences of the conduct and related behavior? Did management, the Board or committees consisting solely of outside directors oversee the review? Did company employees or outside persons perform the review? If outside persons, had

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they done other work for the company? Where the review was conducted by outside counsel, had management previously engaged such counsel? Were scope limitations placed on the review? If so, what were they?

11. Did the company promptly make available to our staff the results of its review and provide sufficient documentation reflecting its response to the situation? Did the company identify possible violative conduct and evidence with sufficient precision to facilitate prompt enforcement actions against those who violated the law? Did the company produce a thorough and probing written report detailing the findings of its review? Did the company voluntarily disclose information our staff did not directly request and otherwise might not have uncovered? Did the company ask its employees to cooperate with our staff and make all reasonable efforts to secure such cooperation?³

12. What assurances are there that the conduct is unlikely to recur? Did the company adopt and ensure enforcement of new and more effective internal controls and procedures designed to prevent a recurrence of the misconduct? Did the company provide our staff with sufficient information for it to evaluate the company's measures to correct the situation and ensure that the conduct does not recur?

13. Is the company the same company in which the misconduct occurred, or has it changed through a merger or bankruptcy reorganization?

We hope that this Report of Investigation and Commission Statement will further encourage self-policing efforts and will promote more self-reporting, remediation and cooperation with the Commission staff. We welcome the constructive input of all interested persons. We urge those who have contributions to make to direct them to our Division of Enforcement. The public can be confident that all such communications will be fairly evaluated not only by our staff, but also by us. We continue to reassess our enforcement approaches with the aim of maximizing the benefits of our program to investors and the marketplace.

By the Commission (Chairman Pitt, Commissioner Hunt, Commissioner Unger).

Footnotes

¹ *In the Matter of Gisela de Leon-Meredith*, Exchange Act Release No. 44970 (October 23, 2001).

² We note that the federal securities laws and other legal requirements and guidance also promote and even require a certain measure of self-policing, self-reporting and remediation. *See, e.g.,* Section 10A of the Securities Exchange Act of 1934, 15 U.S.C. § 78j-1 (requiring issuers and auditors to report certain illegal conduct to the Commission); *In the Matter of W.R. Grace & Co.*, Exchange Act Release No. 39157 (Sept. 30, 1997) (emphasizing

the affirmative responsibilities of corporate officers and directors to ensure that shareholders receive accurate and complete disclosure of information required by the proxy solicitation and periodic reporting provisions of the federal securities laws); *In the Matter of Cooper Companies, Inc.*, Exchange Act Release No. 35082 (Dec. 12, 1994) (emphasizing responsibility of corporate directors in safeguarding the integrity of a company's public statements and the interests of investors when evidence of fraudulent conduct by corporate management comes to their attention); *In the Matter of John Gutfreund*, Exchange Act Release No. 31554 (Dec. 3, 1992) (sanctions imposed against supervisors at broker-dealer for failing promptly to bring misconduct to attention of the government). See also *Federal Sentencing Guidelines* § 8C2.5(f) & (g) (organization's "culpability score" decreases if organization has an effective program to prevent and detect violations of law or if organization reports offense to governmental authorities prior to imminent threat of disclosure or government investigation and within reasonably prompt time after becoming aware of the offense); *New York Stock Exchange Rules* 342.21 & 351(e) (members and member organizations required to review certain trades for compliance with rules against insider trading and manipulation, to conduct prompt internal investigations of any potentially violative trades, and to report the status and/or results of such internal investigations).

³ In some cases, the desire to provide information to the Commission staff may cause companies to consider choosing not to assert the attorney-client privilege, the work product protection and other privileges, protections and exemptions with respect to the Commission. The Commission recognizes that these privileges, protections and exemptions serve important social interests. In this regard, the Commission does not view a company's waiver of a privilege as an end in itself, but only as a means (where necessary) to provide relevant and sometimes critical information to the Commission staff. Thus, the Commission recently filed an *amicus* brief arguing that the provision of privileged information to the Commission staff pursuant to a confidentiality agreement did not necessarily waive the privilege as to third parties. *Brief of SEC as Amicus Curiae, McKesson HBOC, Inc.*, No. 99-C-7980-3 (Ga. Ct. App. Filed May 13, 2001). Moreover, in certain circumstances, the Commission staff has agreed that a witness' production of privileged information would not constitute a subject matter waiver that would entitle the staff to receive further privileged information.

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U.S. Securities and Exchange Commission

Statement of the Securities and Exchange Commission Concerning Financial Penalties

**FOR IMMEDIATE RELEASE
2006-4**

Washington, D.C., Jan. 4, 2006 – The U.S. Securities and Exchange Commission today issued the following statement concerning financial penalties:

Today the Commission announced the filing of two settled actions against corporate issuers, *SEC v. McAfee, Inc.* and *In the Matter of Applix, Inc.* In one, the company will pay a civil money penalty; in the other, a penalty is not part of the settlement.

The question of whether, and if so to what extent, to impose civil penalties against a corporation raises significant questions for our mission of investor protection. The authority to impose such penalties is relatively recent in the Commission's history, and the use of very large corporate penalties is more recent still. Recent cases have not produced a clear public view of when and how the Commission will use corporate penalties, and within the Commission itself a variety of views have heretofore been expressed, but not reconciled.

The Commission believes it important to provide the maximum possible degree of clarity, consistency, and predictability in explaining the way that its corporate penalty authority will be exercised. To this end, we are issuing this statement describing with particularity the framework for our penalty determinations in these two cases. We have issued these decisions, and this statement of principles, unanimously.

In determining whether or not to impose penalties against the corporations in these cases, we carefully considered our statutory authority, and the legislative history surrounding that statutory authority.

In 1990, Congress passed the Securities Enforcement Remedies and Penny Stock Reform Act (the "Remedies Act"), which gave the Commission authority generally to seek civil money penalties in enforcement cases.¹ The penalty provisions added by the Remedies Act expressly authorize the Commission to obtain money penalties from entities, including corporate issuers. These provisions also enhanced the Commission's authority to fine individuals. Today, we limit our discussion to penalties against corporations, although we view penalties against individual offenders as a critical component in punishing and deterring violative conduct.

The Remedies Act legislative history contains express references to penalty assessments against corporate issuers of securities. In its Report on the legislation, the Senate Committee on Banking, Housing, and Urban Affairs

expressly noted both that the civil money penalty provisions would be applicable to corporate issuers, and that shareholders ultimately may bear the cost of penalties imposed on corporate issuers. According to the Report, such penalties should be assessed when the securities law violation that is the basis of the penalty has resulted in an improper benefit to the shareholders. It also cautioned that the Commission and courts should, in considering corporate issuer penalties, take into account whether the penalty would be paid by shareholders who had been the principal victims of the violation:

"The Committee believes that the civil money penalty provisions should be applicable to corporate issuers, and the legislation permits penalties against issuers. However, because the costs of such penalties may be passed on to shareholders, the Committee intends that a penalty be sought when the violation results in an improper benefit to shareholders. In cases in which shareholders are the principal victims of the violations, the Committee expects that the SEC, when appropriate, will seek penalties from the individual offenders acting for a corporate issuer. Moreover, in deciding whether and to what extent to assess a penalty against the issuer, the court may properly take into account whether civil penalties assessed against corporate issuers will ultimately be paid by shareholders who were themselves victimized by the violations. The court also may consider the extent to which the passage of time has resulted in shareholder turnover."²

As this discussion indicates, a key question for the Commission is whether the issuer's violation has provided an improper benefit to the shareholders, or conversely whether the violation has resulted in harm to the shareholders. Where shareholders have been victimized by the violative conduct, or by the resulting negative effect on the entity following its discovery, the Commission is expected to seek penalties from culpable individual offenders acting for a corporation. This same point was made in the SEC's memorandum in support of the Remedies Act, which the then Chairman of the SEC, David Ruder, transmitted to the Senate in a January 18, 1989 letter.³

In addition to the benefit or harm to shareholders, the statute and its legislative history suggest several other factors that may be pertinent to the analysis of corporate issuer penalties. For example, the need for effective deterrence is discussed throughout the legislative history of the Remedies Act.⁴ The Senate Report also notes the importance of good compliance programs and observes that the availability of penalties may encourage development of such programs.⁵ The Senate Report also observes that penalties may serve to decrease the temptation to violate the law in areas where the perceived risk of detection of wrongdoing is small.⁶ Other factors discussed in the legislative history include whether there was fraudulent intent, harm to innocent third parties, and the possibility of unjust enrichment to the wrongdoer.⁷

The Sarbanes-Oxley Act of 2002 changed the ultimate disposition of penalties. Section 308 of Sarbanes-Oxley (the Fair Funds provision) allows the Commission to take penalties paid by individuals and entities in enforcement actions and add them to disgorgement funds for the benefit of

victims. Penalty moneys no longer always go to the Treasury. Under Fair Funds, penalty moneys instead can be used to compensate the victims for the losses they experienced from the wrongdoing. If the victims are shareholders of the corporation being penalized, they will still bear the cost of issuer penalty payments (which is the case with any penalty against a corporate entity). When penalty moneys are ultimately returned to all or some of the investors who were victims of the violation, the amounts returned are less the administrative costs of the distribution. While the legislative history of the Fair Funds provision is scant, there are two general points that can be discerned. First, the purpose of the provision is to provide an additional source of compensation to victims of securities law violations. Second, the provision applies to all penalties and makes no distinction between penalties against individuals or entities.⁸

We have considered the legislative histories of both the Remedies Act and the Fair Funds provisions of the Sarbanes-Oxley Act in reaching the decisions we announce today.

We proceed from the fundamental principle that corporate penalties are an essential part of an aggressive and comprehensive program to enforce the federal securities laws, and that the availability of a corporate penalty, as one of a range of remedies, contributes to the Commission's ability to achieve an appropriate level of deterrence through its decision in a particular case.

With this principle in mind, our view of the appropriateness of a penalty on the corporation in a particular case, as distinct from the individuals who commit a securities law violation, turns principally on two considerations:

The presence or absence of a direct benefit to the corporation as a result of the violation. The fact that a corporation itself has received a direct and material benefit from the offense, for example through reduced expenses or increased revenues, weighs in support of the imposition of a corporate penalty. If the corporation is in any other way unjustly enriched, this similarly weighs in support of the imposition of a corporate penalty. Within this parameter, the strongest case for the imposition of a corporate penalty is one in which the shareholders of the corporation have received an improper benefit as a result of the violation; the weakest case is one in which the current shareholders of the corporation are the principal victims of the securities law violation.

The degree to which the penalty will recompense or further harm the injured shareholders. Because the protection of innocent investors is a principal objective of the securities laws, the imposition of a penalty on the corporation itself carries with it the risk that shareholders who are innocent of the violation will nonetheless bear the burden of the penalty. In some cases, however, the penalty itself may be used as a source of funds to recompense the injury suffered by victims of the securities law violations. The presence of an opportunity to use the penalty as a meaningful source of compensation to injured shareholders is a factor in support of its imposition. The likelihood a corporate penalty will unfairly injure investors, the corporation, or third parties weighs against its use as a sanction.

In addition to these two principal considerations, there are several additional factors that are properly considered in determining whether to

impose a penalty on the corporation. These are:

The need to deter the particular type of offense. The likelihood that a corporate penalty will serve as a strong deterrent to others similarly situated weighs in favor of the imposition of a corporate penalty. Conversely, the prevalence of unique circumstances that render the particular offense unlikely to be repeated in other contexts is a factor weighing against the need for a penalty on the corporation rather than on the responsible individuals.

The extent of the injury to innocent parties. The egregiousness of the harm done, the number of investors injured, and the extent of societal harm if the corporation's infliction of such injury on innocent parties goes unpunished, are significant determinants of the propriety of a corporate penalty.

Whether complicity in the violation is widespread throughout the corporation. The more pervasive the participation in the offense by responsible persons within the corporation, the more appropriate is the use of a corporate penalty. Conversely, within this parameter, isolated conduct by only a few individuals would tend not to support the imposition of a corporate penalty. Whether the corporation has replaced those persons responsible for the violation will also be considered in weighing this factor.

The level of intent on the part of the perpetrators. Within this parameter, the imposition of a corporate penalty is most appropriate in egregious circumstances, where the culpability and fraudulent intent of the perpetrators are manifest. A corporate penalty is less likely to be imposed if the violation is not the result of deliberate, intentionally fraudulent conduct.

The degree of difficulty in detecting the particular type of offense. Because offenses that are particularly difficult to detect call for an especially high level of deterrence, this factor weighs in support of the imposition of a corporate penalty.

Presence or lack of remedial steps by the corporation. Because the aim of the securities laws is to protect investors, the prevention of future harm, as well as the punishment of past offenses, is a high priority. The Commission's decisions in particular cases are intended to encourage the management of corporations accused of securities law violations to do everything within their power to take remedial steps, from the first moment that the violation is brought to their attention. Exemplary conduct by management in this respect weighs against the use of a corporate penalty; failure of management to take remedial steps is a factor supporting the imposition of a corporate penalty.

Extent of cooperation with Commission and other law enforcement. Effective compliance with the securities laws depends upon vigilant supervision, monitoring, and reporting of violations. When securities law violations are discovered, it is incumbent upon management to report them to the Commission and to other appropriate law enforcement authorities. The degree to which a corporation has self reported an offense, or otherwise cooperated with the investigation and remediation of the offense, is a factor that the Commission will consider in determining the propriety of a corporate penalty.

This framework for the consideration of the propriety of corporate penalties is grounded in the Commission's statutory authority and supported by the legislative history underlying that authority. It is the Commission's intent that the elucidation of these principles will provide a high degree of transparency to our decisions in these and future cases, and will be of assistance to the Commission's professional staff, to corporate issuers and their counsel, and to the public.

#

¹ Before the enactment of the Remedies Act, the Commission's penalty authority was essentially limited to the ability to seek penalties in district court for insider trading violations.

² S. Rep. No. 337, 101st Cong., 2d Sess. at 17 (1990) ("1990 Senate Report").

³ *Securities Law Enforcement: Hearings on H.R. 975 Before the Subcomm. on Telecommunications and Finance of the House Comm. on Energy and Commerce*, 101st Cong., 1st Sess. 47-48 (1989) (statement of David S. Ruder, Chairman, SEC, attaching Memorandum of the SEC in Support of the Securities Law Enforcement Remedies Act of 1989).

⁴ See, e.g., 1990 Senate Report at 6-11; see also Section 21B(c)(5) of the Exchange Act.

⁵ 1990 Senate Report at 10-11.

⁶ 1990 Senate Report at 15.

⁷ 1990 Senate Report at 14. See, e.g., Section 21B(c)(1)-(3) of the Exchange Act.

⁸ See House Committee on Financial Services Release, "Baker Proposes FAIR Account to Return Funds to Defrauded Investors" (July 17, 2002) (including statements of Chairman Oxley and Chairman Baker), available at <http://financialservices.house.gov/news.asp>.

Additional materials:

- ▶ [Litigation Release 19520](#)
- ▶ [Administrative Proceeding Release No. 33-8651](#)

<http://www.sec.gov/news/press/2006-4.htm>

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Appendix F

**Whistleblower Provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act
H.R. 4173, 111th Cong. (2010)**

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H. R. 4173

One Hundred Eleventh Congress
of the
United States of America

AT THE SECOND SESSION

*Begun and held at the City of Washington on Tuesday,
the fifth day of January, two thousand and ten*

An Act

To promote the financial stability of the United States by improving accountability and transparency in the financial system, to end "too big to fail", to protect the American taxpayer by ending bailouts, to protect consumers from abusive financial services practices, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE; TABLE OF CONTENTS.

(a) **SHORT TITLE.**—This Act may be cited as the "Dodd-Frank Wall Street Reform and Consumer Protection Act".

(b) **TABLE OF CONTENTS.**—The table of contents for this Act is as follows:

- Sec. 1. Short title; table of contents.
- Sec. 2. Definitions.
- Sec. 3. Severability.
- Sec. 4. Effective date.
- Sec. 5. Budgetary effects.
- Sec. 6. Antitrust savings clause.

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- Sec. 115. Enhanced supervision and prudential standards for nonbank financial companies supervised by the Board of Governors and certain bank holding companies.
- Sec. 116. Reports.
- Sec. 117. Treatment of certain companies that cease to be bank holding companies.
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- Sec. 119. Resolution of supervisory jurisdictional disputes among member agencies.
- Sec. 120. Additional standards applicable to activities or practices for financial stability purposes.
- Sec. 121. Mitigation of risks to financial stability.
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- Sec. 123. Study of the effects of size and complexity of financial institutions on capital market efficiency and economic growth.

Subtitle B—Office of Financial Research

- Sec. 151. Definitions.
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- Sec. 154. Organizational structure; responsibilities of primary programmatic units.
- Sec. 155. Funding.
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- Sec. 161. Reports by and examinations of nonbank financial companies by the Board of Governors.
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- Sec. 172. Examination and enforcement actions for insurance and orderly liquidation purposes.
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- Sec. 201. Definitions.
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- Sec. 207. Directors not liable for acquiescing in appointment of receiver.
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- Sec. 1491. Sense of Congress regarding the importance of government-sponsored enterprises reform to enhance the protection, limitation, and regulation of the terms of residential mortgage credit.
 Sec. 1492. GAO study report on government efforts to combat mortgage foreclosure rescue scams and loan modification fraud.
 Sec. 1493. Reporting of mortgage data by State.
 Sec. 1494. Study of effect of drywall presence on foreclosures.
 Sec. 1495. Definition.
 Sec. 1496. Emergency mortgage relief.
 Sec. 1497. Additional assistance for Neighborhood Stabilization Program.
 Sec. 1498. Legal assistance for foreclosure-related issues.

TITLE XV—MISCELLANEOUS PROVISIONS

- Sec. 1501. Restrictions on use of United States funds for foreign governments; protection of American taxpayers.
 Sec. 1502. Conflict minerals.
 Sec. 1503. Reporting requirements regarding coal or other mine safety.
 Sec. 1504. Disclosure of payments by resource extraction issuers.
 Sec. 1505. Study by the Comptroller General.
 Sec. 1506. Study on core deposits and brokered deposits.

TITLE XVI—SECTION 1256 CONTRACTS

- Sec. 1601. Certain swaps, etc., not treated as section 1256 contracts.

SEC. 2. DEFINITIONS.

As used in this Act, the following definitions shall apply, except as the context otherwise requires or as otherwise specifically provided in this Act:

(1) **AFFILIATE.**—The term “affiliate” has the same meaning as in section 3 of the Federal Deposit Insurance Act (12 U.S.C. 1813).

(2) **APPROPRIATE FEDERAL BANKING AGENCY.**—On and after the transfer date, the term “appropriate Federal banking agency” has the same meaning as in section 3(q) of the Federal Deposit Insurance Act (12 U.S.C. 1813(q)), as amended by title III.

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holding or creating the information in a manner which makes it generally available to the trading public, or disclosed in a criminal, civil, or administrative hearing, or in a congressional, administrative, or Government Accountability Office report, hearing, audit, or investigation, and to use such information, or to impart such information with the intent to assist another person, directly or indirectly, to use such information to enter into, or offer to enter into—

“(i) a contract of sale of a commodity for future delivery (or option on such a contract);

“(ii) an option (other than an option executed or traded on a national securities exchange registered pursuant to section 6(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78f(a)); or

“(iii) a swap, provided, however, that nothing in this subparagraph shall preclude a person that has provided information concerning, or generated by, the person, its operations or activities, to any employee or agent of any department or agency of the Federal Government, voluntarily or as required by law, from using such information to enter into, or offer to enter into, a contract of sale, option, or swap described in clauses (i), (ii), or (iii).”.

SEC. 747. ANTIDISRUPTIVE PRACTICES AUTHORITY.

Section 4c(a) of the Commodity Exchange Act (7 U.S.C. 6c(a)) (as amended by section 746) is amended by adding at the end the following:

“(5) **DISRUPTIVE PRACTICES.**—It shall be unlawful for any person to engage in any trading, practice, or conduct on or subject to the rules of a registered entity that—

“(A) violates bids or offers;

“(B) demonstrates intentional or reckless disregard for the orderly execution of transactions during the closing period; or

“(C) is, is of the character of, or is commonly known to the trade as, ‘spoofing’ (bidding or offering with the intent to cancel the bid or offer before execution).

“(6) **RULEMAKING AUTHORITY.**—The Commission may make and promulgate such rules and regulations as, in the judgment of the Commission, are reasonably necessary to prohibit the trading practices described in paragraph (5) and any other trading practice that is disruptive of fair and equitable trading.

“(7) **USE OF SWAPS TO DEFRAUD.**—It shall be unlawful for any person to enter into a swap knowing, or acting in reckless disregard of the fact, that its counterparty will use the swap as part of a device, scheme, or artifice to defraud any third party.”.

SEC. 748. COMMODITY WHISTLEBLOWER INCENTIVES AND PROTECTION.

The Commodity Exchange Act (7 U.S.C. 1 et seq.) is amended by adding at the end the following:

“SEC. 23. COMMODITY WHISTLEBLOWER INCENTIVES AND PROTECTION.

“(a) **DEFINITIONS.**—In this section:

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"(1) COVERED JUDICIAL OR ADMINISTRATIVE ACTION.—The term 'covered judicial or administrative action' means any judicial or administrative action brought by the Commission under this Act that results in monetary sanctions exceeding \$1,000,000.

"(2) FUND.—The term 'Fund' means the Commodity Futures Trading Commission Customer Protection Fund established under subsection (g).

"(3) MONETARY SANCTIONS.—The term 'monetary sanctions', when used with respect to any judicial or administrative action means—

"(A) any monies, including penalties, disgorgement, restitution, and interest ordered to be paid; and

"(B) any monies deposited into a disgorgement fund or other fund pursuant to section 308(b) of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7246(b)), as a result of such action or any settlement of such action.

"(4) ORIGINAL INFORMATION.—The term 'original information' means information that—

"(A) is derived from the independent knowledge or analysis of a whistleblower;

"(B) is not known to the Commission from any other source, unless the whistleblower is the original source of the information; and

"(C) is not exclusively derived from an allegation made in a judicial or administrative hearing, in a governmental report, hearing, audit, or investigation, or from the news media, unless the whistleblower is a source of the information.

"(5) RELATED ACTION.—The term 'related action', when used with respect to any judicial or administrative action brought by the Commission under this Act, means any judicial or administrative action brought by an entity described in subclauses (I) through (VI) of subsection (h)(2)(C) that is based upon the original information provided by a whistleblower pursuant to subsection (a) that led to the successful enforcement of the Commission action.

"(6) SUCCESSFUL RESOLUTION.—The term 'successful resolution', when used with respect to any judicial or administrative action brought by the Commission under this Act, includes any settlement of such action.

"(7) WHISTLEBLOWER.—The term 'whistleblower' means any individual, or 2 or more individuals acting jointly, who provides information relating to a violation of this Act to the Commission, in a manner established by rule or regulation by the Commission.

"(b) AWARDS.—

"(1) IN GENERAL.—In any covered judicial or administrative action, or related action, the Commission, under regulations prescribed by the Commission and subject to subsection (c), shall pay an award or awards to 1 or more whistleblowers who voluntarily provided original information to the Commission that led to the successful enforcement of the covered judicial or administrative action, or related action, in an aggregate amount equal to—

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“(A) not less than 10 percent, in total, of what has been collected of the monetary sanctions imposed in the action or related actions; and

“(B) not more than 30 percent, in total, of what has been collected of the monetary sanctions imposed in the action or related actions.

“(2) PAYMENT OF AWARDS.—Any amount paid under paragraph (1) shall be paid from the Fund.

“(c) DETERMINATION OF AMOUNT OF AWARD; DENIAL OF AWARD.—

“(1) DETERMINATION OF AMOUNT OF AWARD.—

“(A) DISCRETION.—The determination of the amount of an award made under subsection (b) shall be in the discretion of the Commission.

“(B) CRITERIA.—In determining the amount of an award made under subsection (b), the Commission—

“(i) shall take into consideration—

“(I) the significance of the information provided by the whistleblower to the success of the covered judicial or administrative action;

“(II) the degree of assistance provided by the whistleblower and any legal representative of the whistleblower in a covered judicial or administrative action;

“(III) the programmatic interest of the Commission in deterring violations of the Act (including regulations under the Act) by making awards to whistleblowers who provide information that leads to the successful enforcement of such laws; and

“(IV) such additional relevant factors as the Commission may establish by rule or regulation; and

“(ii) shall not take into consideration the balance of the Fund.

“(2) DENIAL OF AWARD.—No award under subsection (b) shall be made—

“(A) to any whistleblower who is, or was at the time the whistleblower acquired the original information submitted to the Commission, a member, officer, or employee of—

“(i) a appropriate regulatory agency;

“(ii) the Department of Justice;

“(iii) a registered entity;

“(iv) a registered futures association;

“(v) a self-regulatory organization as defined in section 3(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)); or

“(vi) a law enforcement organization;

“(B) to any whistleblower who is convicted of a criminal violation related to the judicial or administrative action for which the whistleblower otherwise could receive an award under this section;

“(C) to any whistleblower who submits information to the Commission that is based on the facts underlying the covered action submitted previously by another whistleblower;

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“(D) to any whistleblower who fails to submit information to the Commission in such form as the Commission may, by rule or regulation, require.

“(d) REPRESENTATION.—

“(1) PERMITTED REPRESENTATION.—Any whistleblower who makes a claim for an award under subsection (b) may be represented by counsel.

“(2) REQUIRED REPRESENTATION.—

“(A) IN GENERAL.—Any whistleblower who anonymously makes a claim for an award under subsection (b) shall be represented by counsel if the whistleblower submits the information upon which the claim is based.

“(B) DISCLOSURE OF IDENTITY.—Prior to the payment of an award, a whistleblower shall disclose the identity of the whistleblower and provide such other information as the Commission may require, directly or through counsel for the whistleblower.

“(e) NO CONTRACT NECESSARY.—No contract with the Commission is necessary for any whistleblower to receive an award under subsection (b), unless otherwise required by the Commission, by rule or regulation.

“(f) APPEALS.—

“(1) IN GENERAL.—Any determination made under this section, including whether, to whom, or in what amount to make awards, shall be in the discretion of the Commission.

“(2) APPEALS.—Any determination described in paragraph (1) may be appealed to the appropriate court of appeals of the United States not more than 30 days after the determination is issued by the Commission.

“(3) REVIEW.—The court shall review the determination made by the Commission in accordance with section 7064 of title 5, United States Code.

“(g) COMMODITY FUTURES TRADING COMMISSION CUSTOMER PROTECTION FUND.—

“(1) ESTABLISHMENT.—There is established in the Treasury of the United States a revolving fund to be known as the ‘Commodity Futures Trading Commission Customer Protection Fund’.

“(2) USE OF FUND.—The Fund shall be available to the Commission, without further appropriation or fiscal year limitation, for—

“(A) the payment of awards to whistleblowers as provided in subsection (a); and

“(B) the funding of customer education initiatives designed to help customers protect themselves against fraud or other violations of this Act, or the rules and regulations thereunder.

“(3) DEPOSITS AND CREDITS.—There shall be deposited into or credited to the Fund:

“(A) MONETARY SANCTIONS.—Any monetary sanctions collected by the Commission in any covered judicial or administrative action that is not otherwise distributed to victims of a violation of this Act or the rules and regulations thereunder underlying such action, unless the balance of the Fund at the time the monetary judgment is collected exceeds \$100,000,000.

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"(B) ADDITIONAL AMOUNTS.—If the amounts deposited into or credited to the Fund under subparagraph (A) are not sufficient to satisfy an award made under subsection (b), there shall be deposited into or credited to the Fund an amount equal to the unsatisfied portion of the award from any monetary sanction collected by the Commission in any judicial or administrative action brought by the Commission under this Act that is based on information provided by a whistleblower.

"(C) INVESTMENT INCOME.—All income from investments made under paragraph (4).

"(4) INVESTMENTS.—

"(A) AMOUNTS IN FUND MAY BE INVESTED.—The Commission may request the Secretary of the Treasury to invest the portion of the Fund that is not, in the Commission's judgment, required to meet the current needs of the Fund.

"(B) ELIGIBLE INVESTMENTS.—Investments shall be made by the Secretary of the Treasury in obligations of the United States or obligations that are guaranteed as to principal and interest by the United States, with maturities suitable to the needs of the Fund as determined by the Commission.

"(C) INTEREST AND PROCEEDS CREDITED.—The interest on, and the proceeds from the sale or redemption of, any obligations held in the Fund shall be credited to, and form a part of, the Fund.

"(5) REPORTS TO CONGRESS.—Not later than October 30 of each year, the Commission shall transmit to the Committee on Agriculture, Nutrition, and Forestry of the Senate, and the Committee on Agriculture of the House of Representatives a report on—

"(A) the Commission's whistleblower award program under this section, including a description of the number of awards granted and the types of cases in which awards were granted during the preceding fiscal year;

"(B) customer education initiatives described in paragraph (2)(B) that were funded by the Fund during the preceding fiscal year;

"(C) the balance of the Fund at the beginning of the preceding fiscal year;

"(D) the amounts deposited into or credited to the Fund during the preceding fiscal year;

"(E) the amount of earnings on investments of amounts in the Fund during the preceding fiscal year;

"(F) the amount paid from the Fund during the preceding fiscal year to whistleblowers pursuant to subsection (b);

"(G) the amount paid from the Fund during the preceding fiscal year for customer education initiatives described in paragraph (2)(B);

"(H) the balance of the Fund at the end of the preceding fiscal year; and

"(I) a complete set of audited financial statements, including a balance sheet, income statement, and cash flow analysis.

"(h) PROTECTION OF WHISTLEBLOWERS.—

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"(1) PROHIBITION AGAINST RETALIATION.—

"(A) IN GENERAL.—No employer may discharge, demote, suspend, threaten, harass, directly or indirectly, or in any other manner discriminate against, a whistleblower in the terms and conditions of employment because of any lawful act done by the whistleblower—

"(i) in providing information to the Commission in accordance with subsection (b); or

"(ii) in assisting in any investigation or judicial or administrative action of the Commission based upon or related to such information.

"(B) ENFORCEMENT.—

"(i) CAUSE OF ACTION.—An individual who alleges discharge or other discrimination in violation of subparagraph (A) may bring an action under this subsection in the appropriate district court of the United States for the relief provided in subparagraph (C), unless the individual who is alleging discharge or other discrimination in violation of subparagraph (A) is an employee of the Federal Government, in which case the individual shall only bring an action under section 1221 of title 5, United States Code.

"(ii) SUBPOENAS.—A subpoena requiring the attendance of a witness at a trial or hearing conducted under this subsection may be served at any place in the United States.

"(iii) STATUTE OF LIMITATIONS.—An action under this subsection may not be brought more than 2 years after the date on which the violation reported in subparagraph (A) is committed.

"(C) RELIEF.—Relief for an individual prevailing in an action brought under subparagraph (B) shall include—

"(i) reinstatement with the same seniority status that the individual would have had, but for the discrimination;

"(ii) the amount of back pay otherwise owed to the individual, with interest; and

"(iii) compensation for any special damages sustained as a result of the discharge or discrimination, including litigation costs, expert witness fees, and reasonable attorney's fees.

"(2) CONFIDENTIALITY.—

"(A) IN GENERAL.—Except as provided in subparagraphs (B) and (C), the Commission, and any officer or employee of the Commission, shall not disclose any information, including information provided by a whistleblower to the Commission, which could reasonably be expected to reveal the identity of a whistleblower, except in accordance with the provisions of section 552a of title 5, United States Code, unless and until required to be disclosed to a defendant or respondent in connection with a public proceeding instituted by the Commission or any entity described in subparagraph (C). For purposes of section 552 of title 5, United States Code, this paragraph shall be considered a statute described in subsection (b)(3)(B) of such section 552.

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“(B) EFFECT.—Nothing in this paragraph is intended to limit the ability of the Attorney General to present such evidence to a grand jury or to share such evidence with potential witnesses or defendants in the course of an ongoing criminal investigation.

“(C) AVAILABILITY TO GOVERNMENT AGENCIES.—

“(i) IN GENERAL.—Without the loss of its status as confidential in the hands of the Commission, all information referred to in subparagraph (A) may, in the discretion of the Commission, when determined by the Commission to be necessary or appropriate to accomplish the purposes of this Act and protect customers and in accordance with clause (ii), be made available to—

“(I) the Department of Justice;

“(II) an appropriate department or agency of the Federal Government, acting within the scope of its jurisdiction;

“(III) a registered entity, registered futures association, or self-regulatory organization as defined in section 3(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a));

“(IV) a State attorney general in connection with any criminal investigation;

“(V) an appropriate department or agency of any State, acting within the scope of its jurisdiction; and

“(VI) a foreign futures authority.

“(ii) MAINTENANCE OF INFORMATION.—Each of the entities, agencies, or persons described in clause (i) shall maintain information described in that clause as confidential, in accordance with the requirements in subparagraph (A).

“(iii) STUDY ON IMPACT OF FOIA EXEMPTION ON COMMODITY FUTURES TRADING COMMISSION.—

“(I) STUDY.—The Inspector General of the Commission shall conduct a study—

“(aa) on whether the exemption under section 552(b)(3) of title 5, United States Code (known as the Freedom of Information Act) established in paragraph (2)(A) aids whistleblowers in disclosing information to the Commission;

“(bb) on what impact the exemption has had on the public's ability to access information about the Commission's regulation of commodity futures and option markets; and

“(cc) to make any recommendations on whether the Commission should continue to use the exemption.

“(II) REPORT.—Not later than 30 months after the date of enactment of this clause, the Inspector General shall—

“(aa) submit a report on the findings of the study required under this clause to the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on

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Financial Services of the House of Representatives; and

“(bb) make the report available to the public through publication of a report on the website of the Commission.

“(3) RIGHTS RETAINED.—Nothing in this section shall be deemed to diminish the rights, privileges, or remedies of any whistleblower under any Federal or State law, or under any collective bargaining agreement.

“(i) RULEMAKING AUTHORITY.—The Commission shall have the authority to issue such rules and regulations as may be necessary or appropriate to implement the provisions of this section consistent with the purposes of this section.

“(j) IMPLEMENTING RULES.—The Commission shall issue final rules or regulations implementing the provisions of this section not later than 270 days after the date of enactment of the Wall Street Transparency and Accountability Act of 2010.

“(k) ORIGINAL INFORMATION.—Information submitted to the Commission by a whistleblower in accordance with rules or regulations implementing this section shall not lose its status as original information solely because the whistleblower submitted such information prior to the effective date of such rules or regulations, provided such information was submitted after the date of enactment of the Wall Street Transparency and Accountability Act of 2010.

“(l) AWARDS.—A whistleblower may receive an award pursuant to this section regardless of whether any violation of a provision of this Act, or a rule or regulation thereunder, underlying the judicial or administrative action upon which the award is based occurred prior to the date of enactment of the Wall Street Transparency and Accountability Act of 2010.

“(m) PROVISION OF FALSE INFORMATION.—A whistleblower who knowingly and willfully makes any false, fictitious, or fraudulent statement or representation, or who makes or uses any false writing or document knowing the same to contain any false, fictitious, or fraudulent statement or entry, shall not be entitled to an award under this section and shall be subject to prosecution under section 1001 of title 18, United States Code.

“(n) NONENFORCEABILITY OF CERTAIN PROVISIONS WAIVING RIGHTS AND REMEDIES OR REQUIRING ARBITRATION OF DISPUTES.—

“(1) WAIVER OF RIGHTS AND REMEDIES.—The rights and remedies provided for in this section may not be waived by any agreement, policy form, or condition of employment including by a predispute arbitration agreement.

“(2) PREDISPUTE ARBITRATION AGREEMENTS.—No predispute arbitration agreement shall be valid or enforceable, if the agreement requires arbitration of a dispute arising under this section.”.

SEC. 749. CONFORMING AMENDMENTS.

(a) Section 4d of the Commodity Exchange Act (7 U.S.C. 6d) (as amended by section 724) is amended—

(1) in subsection (a)—

(A) in the matter preceding paragraph (1)—

(i) by striking “engage as” and inserting “be a”;

and

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activities and evaluates the effectiveness of the Ombudsman during the preceding year. The Investor Advocate shall include the reports required under this section in the reports required to be submitted by the Inspector Advocate under paragraph (6).”

Subtitle B—Increasing Regulatory Enforcement and Remedies

SEC. 921. AUTHORITY TO RESTRICT MANDATORY PRE-DISPUTE ARBITRATION.

(a) AMENDMENT TO SECURITIES EXCHANGE ACT OF 1934.—Section 15 of the Securities Exchange Act of 1934 (15 U.S.C. 78o), as amended by this title, is further amended by adding at the end the following new subsection:

“(o) AUTHORITY TO RESTRICT MANDATORY PRE-DISPUTE ARBITRATION.—The Commission, by rule, may prohibit, or impose conditions or limitations on the use of, agreements that require customers or clients of any broker, dealer, or municipal securities dealer to arbitrate any future dispute between them arising under the Federal securities laws, the rules and regulations thereunder, or the rules of a self-regulatory organization if it finds that such prohibition, imposition of conditions, or limitations are in the public interest and for the protection of investors.”

(b) AMENDMENT TO INVESTMENT ADVISERS ACT OF 1940.—Section 205 of the Investment Advisers Act of 1940 (15 U.S.C. 80b-5) is amended by adding at the end the following new subsection:

“(f) AUTHORITY TO RESTRICT MANDATORY PRE-DISPUTE ARBITRATION.—The Commission, by rule, may prohibit, or impose conditions or limitations on the use of, agreements that require customers or clients of any investment adviser to arbitrate any future dispute between them arising under the Federal securities laws, the rules and regulations thereunder, or the rules of a self-regulatory organization if it finds that such prohibition, imposition of conditions, or limitations are in the public interest and for the protection of investors.”

SEC. 922. WHISTLEBLOWER PROTECTION.

(a) IN GENERAL.—The Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) is amended by inserting after section 21E the following:

“SEC. 21F. SECURITIES WHISTLEBLOWER INCENTIVES AND PROTECTION.

“(a) DEFINITIONS.—In this section the following definitions shall apply:

“(1) COVERED JUDICIAL OR ADMINISTRATIVE ACTION.—The term ‘covered judicial or administrative action’ means any judicial or administrative action brought by the Commission under the securities laws that results in monetary sanctions exceeding \$1,000,000.

“(2) FUND.—The term ‘Fund’ means the Securities and Exchange Commission Investor Protection Fund.

“(3) ORIGINAL INFORMATION.—The term ‘original information’ means information that—

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“(A) is derived from the independent knowledge or analysis of a whistleblower;

“(B) is not known to the Commission from any other source, unless the whistleblower is the original source of the information; and

“(C) is not exclusively derived from an allegation made in a judicial or administrative hearing, in a governmental report, hearing, audit, or investigation, or from the news media, unless the whistleblower is a source of the information.

“(4) MONETARY SANCTIONS.—The term ‘monetary sanctions’, when used with respect to any judicial or administrative action, means—

“(A) any monies, including penalties, disgorgement, and interest, ordered to be paid; and

“(B) any monies deposited into a disgorgement fund or other fund pursuant to section 308(b) of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7246(b)), as a result of such action or any settlement of such action.

“(5) RELATED ACTION.—The term ‘related action’, when used with respect to any judicial or administrative action brought by the Commission under the securities laws, means any judicial or administrative action brought by an entity described in subclauses (I) through (IV) of subsection (h)(2)(D)(i) that is based upon the original information provided by a whistleblower pursuant to subsection (a) that led to the successful enforcement of the Commission action.

“(6) WHISTLEBLOWER.—The term ‘whistleblower’ means any individual who provides, or 2 or more individuals acting jointly who provide, information relating to a violation of the securities laws to the Commission, in a manner established, by rule or regulation, by the Commission.

“(b) AWARDS.—

“(1) IN GENERAL.—In any covered judicial or administrative action, or related action, the Commission, under regulations prescribed by the Commission and subject to subsection (c), shall pay an award or awards to 1 or more whistleblowers who voluntarily provided original information to the Commission that led to the successful enforcement of the covered judicial or administrative action, or related action, in an aggregate amount equal to—

“(A) not less than 10 percent, in total, of what has been collected of the monetary sanctions imposed in the action or related actions; and

“(B) not more than 30 percent, in total, of what has been collected of the monetary sanctions imposed in the action or related actions.

“(2) PAYMENT OF AWARDS.—Any amount paid under paragraph (1) shall be paid from the Fund.

“(c) DETERMINATION OF AMOUNT OF AWARD; DENIAL OF AWARD.—

“(1) DETERMINATION OF AMOUNT OF AWARD.—

“(A) DISCRETION.—The determination of the amount of an award made under subsection (b) shall be in the discretion of the Commission.

“(B) CRITERIA.—In determining the amount of an award made under subsection (b), the Commission—

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“(i) shall take into consideration—

“(I) the significance of the information provided by the whistleblower to the success of the covered judicial or administrative action;

“(II) the degree of assistance provided by the whistleblower and any legal representative of the whistleblower in a covered judicial or administrative action;

“(III) the programmatic interest of the Commission in deterring violations of the securities laws by making awards to whistleblowers who provide information that lead to the successful enforcement of such laws; and

“(IV) such additional relevant factors as the Commission may establish by rule or regulation; and

“(ii) shall not take into consideration the balance of the Fund.

“(2) DENIAL OF AWARD.—No award under subsection (b) shall be made—

“(A) to any whistleblower who is, or was at the time the whistleblower acquired the original information submitted to the Commission, a member, officer, or employee of—

“(i) an appropriate regulatory agency;

“(ii) the Department of Justice;

“(iii) a self-regulatory organization;

“(iv) the Public Company Accounting Oversight Board; or

“(v) a law enforcement organization;

“(B) to any whistleblower who is convicted of a criminal violation related to the judicial or administrative action for which the whistleblower otherwise could receive an award under this section;

“(C) to any whistleblower who gains the information through the performance of an audit of financial statements required under the securities laws and for whom such submission would be contrary to the requirements of section 10A of the Securities Exchange Act of 1934 (15 U.S.C. 78j-1); or

“(D) to any whistleblower who fails to submit information to the Commission in such form as the Commission may, by rule, require.

“(d) REPRESENTATION.—

“(1) PERMITTED REPRESENTATION.—Any whistleblower who makes a claim for an award under subsection (b) may be represented by counsel.

“(2) REQUIRED REPRESENTATION.—

“(A) IN GENERAL.—Any whistleblower who anonymously makes a claim for an award under subsection (b) shall be represented by counsel if the whistleblower anonymously submits the information upon which the claim is based.

“(B) DISCLOSURE OF IDENTITY.—Prior to the payment of an award, a whistleblower shall disclose the identity of the whistleblower and provide such other information

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as the Commission may require, directly or through counsel for the whistleblower.

"(e) NO CONTRACT NECESSARY.—No contract with the Commission is necessary for any whistleblower to receive an award under subsection (b), unless otherwise required by the Commission by rule or regulation.

"(f) APPEALS.—Any determination made under this section, including whether, to whom, or in what amount to make awards, shall be in the discretion of the Commission. Any such determination, except the determination of the amount of an award if the award was made in accordance with subsection (b), may be appealed to the appropriate court of appeals of the United States not more than 30 days after the determination is issued by the Commission. The court shall review the determination made by the Commission in accordance with section 706 of title 5, United States Code.

"(g) INVESTOR PROTECTION FUND.—

"(1) FUND ESTABLISHED.—There is established in the Treasury of the United States a fund to be known as the 'Securities and Exchange Commission Investor Protection Fund'.

"(2) USE OF FUND.—The Fund shall be available to the Commission, without further appropriation or fiscal year limitation, for—

"(A) paying awards to whistleblowers as provided in subsection (b); and

"(B) funding the activities of the Inspector General of the Commission under section 4(i).

"(3) DEPOSITS AND CREDITS.—

"(A) IN GENERAL.—There shall be deposited into or credited to the Fund an amount equal to—

"(i) any monetary sanction collected by the Commission in any judicial or administrative action brought by the Commission under the securities laws that is not added to a disgorgement fund or other fund under section 308 of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7246) or otherwise distributed to victims of a violation of the securities laws, or the rules and regulations thereunder, underlying such action, unless the balance of the Fund at the time the monetary sanction is collected exceeds \$300,000,000;

"(ii) any monetary sanction added to a disgorgement fund or other fund under section 308 of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7246) that is not distributed to the victims for whom the Fund was established, unless the balance of the disgorgement fund at the time the determination is made not to distribute the monetary sanction to such victims exceeds \$200,000,000; and

"(iii) all income from investments made under paragraph (4).

"(B) ADDITIONAL AMOUNTS.—If the amounts deposited into or credited to the Fund under subparagraph (A) are not sufficient to satisfy an award made under subsection (b), there shall be deposited into or credited to the Fund an amount equal to the unsatisfied portion of the award from any monetary sanction collected by the Commission

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in the covered judicial or administrative action on which the award is based.

“(4) INVESTMENTS.—

“(A) AMOUNTS IN FUND MAY BE INVESTED.—The Commission may request the Secretary of the Treasury to invest the portion of the Fund that is not, in the discretion of the Commission, required to meet the current needs of the Fund.

“(B) ELIGIBLE INVESTMENTS.—Investments shall be made by the Secretary of the Treasury in obligations of the United States or obligations that are guaranteed as to principal and interest by the United States, with maturities suitable to the needs of the Fund as determined by the Commission on the record.

“(C) INTEREST AND PROCEEDS CREDITED.—The interest on, and the proceeds from the sale or redemption of, any obligations held in the Fund shall be credited to the Fund.

“(5) REPORTS TO CONGRESS.—Not later than October 30 of each fiscal year beginning after the date of enactment of this subsection, the Commission shall submit to the Committee on Banking, Housing, and Urban Affairs of the Senate, and the Committee on Financial Services of the House of Representatives a report on—

“(A) the whistleblower award program, established under this section, including—

“(i) a description of the number of awards granted; and

“(ii) the types of cases in which awards were granted during the preceding fiscal year;

“(B) the balance of the Fund at the beginning of the preceding fiscal year;

“(C) the amounts deposited into or credited to the Fund during the preceding fiscal year;

“(D) the amount of earnings on investments made under paragraph (4) during the preceding fiscal year;

“(E) the amount paid from the Fund during the preceding fiscal year to whistleblowers pursuant to subsection (b);

“(F) the balance of the Fund at the end of the preceding fiscal year; and

“(G) a complete set of audited financial statements, including—

“(i) a balance sheet;

“(ii) income statement; and

“(iii) cash flow analysis.

“(h) PROTECTION OF WHISTLEBLOWERS.—

“(1) PROHIBITION AGAINST RETALIATION.—

“(A) IN GENERAL.—No employer may discharge, demote, suspend, threaten, harass, directly or indirectly, or in any other manner discriminate against, a whistleblower in the terms and conditions of employment because of any lawful act done by the whistleblower—

“(i) in providing information to the Commission in accordance with this section;

“(ii) in initiating, testifying in, or assisting in any investigation or judicial or administrative action of

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the Commission based upon or related to such information; or

"(iii) in making disclosures that are required or protected under the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7201 et seq.), the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.), including section 10A(m) of such Act (15 U.S.C. 78f(m)), section 1513(e) of title 18, United States Code, and any other law, rule, or regulation subject to the jurisdiction of the Commission.

"(B) ENFORCEMENT.—

"(i) CAUSE OF ACTION.—An individual who alleges discharge or other discrimination in violation of subparagraph (A) may bring an action under this subsection in the appropriate district court of the United States for the relief provided in subparagraph (C).

"(ii) SUBPOENAS.—A subpoena requiring the attendance of a witness at a trial or hearing conducted under this section may be served at any place in the United States.

"(iii) STATUTE OF LIMITATIONS.—

"(I) IN GENERAL.—An action under this subsection may not be brought—

"(aa) more than 6 years after the date on which the violation of subparagraph (A) occurred; or

"(bb) more than 3 years after the date when facts material to the right of action are known or reasonably should have been known by the employee alleging a violation of subparagraph (A).

"(II) REQUIRED ACTION WITHIN 10 YEARS.—Notwithstanding subclause (I), an action under this subsection may not in any circumstance be brought more than 10 years after the date on which the violation occurs.

"(C) RELIEF.—Relief for an individual prevailing in an action brought under subparagraph (B) shall include—

"(i) reinstatement with the same seniority status that the individual would have had, but for the discrimination;

"(ii) 2 times the amount of back pay otherwise owed to the individual, with interest; and

"(iii) compensation for litigation costs, expert witness fees, and reasonable attorneys' fees.

"(2) CONFIDENTIALITY.—

"(A) IN GENERAL.—Except as provided in subparagraphs (B) and (C), the Commission and any officer or employee of the Commission shall not disclose any information, including information provided by a whistleblower to the Commission, which could reasonably be expected to reveal the identity of a whistleblower, except in accordance with the provisions of section 552a of title 5, United States Code, unless and until required to be disclosed to a defendant or respondent in connection with a public proceeding instituted by the Commission or any entity described in subparagraph (C). For purposes of section

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552 of title 5, United States Code, this paragraph shall be considered a statute described in subsection (b)(3)(B) of such section.

“(B) EXEMPTED STATUTE.—For purposes of section 552 of title 5, United States Code, this paragraph shall be considered a statute described in subsection (b)(3)(B) of such section 552.

“(C) RULE OF CONSTRUCTION.—Nothing in this section is intended to limit, or shall be construed to limit, the ability of the Attorney General to present such evidence to a grand jury or to share such evidence with potential witnesses or defendants in the course of an ongoing criminal investigation.

“(D) AVAILABILITY TO GOVERNMENT AGENCIES.—

“(i) IN GENERAL.—Without the loss of its status as confidential in the hands of the Commission, all information referred to in subparagraph (A) may, in the discretion of the Commission, when determined by the Commission to be necessary to accomplish the purposes of this Act and to protect investors, be made available to—

“(I) the Attorney General of the United States;

“(II) an appropriate regulatory authority;

“(III) a self-regulatory organization;

“(IV) a State attorney general in connection with any criminal investigation;

“(V) any appropriate State regulatory authority;

“(VI) the Public Company Accounting Oversight Board;

“(VII) a foreign securities authority; and

“(VIII) a foreign law enforcement authority.

“(ii) CONFIDENTIALITY.—

“(I) IN GENERAL.—Each of the entities described in subclauses (I) through (VI) of clause (i) shall maintain such information as confidential in accordance with the requirements established under subparagraph (A).

“(II) FOREIGN AUTHORITIES.—Each of the entities described in subclauses (VII) and (VIII) of clause (i) shall maintain such information in accordance with such assurances of confidentiality as the Commission determines appropriate.

“(3) RIGHTS RETAINED.—Nothing in this section shall be deemed to diminish the rights, privileges, or remedies of any whistleblower under any Federal or State law, or under any collective bargaining agreement.

“(i) PROVISION OF FALSE INFORMATION.—A whistleblower shall not be entitled to an award under this section if the whistleblower—

“(1) knowingly and willfully makes any false, fictitious, or fraudulent statement or representation; or

“(2) uses any false writing or document knowing the writing or document contains any false, fictitious, or fraudulent statement or entry.

“(j) RULEMAKING AUTHORITY.—The Commission shall have the authority to issue such rules and regulations as may be necessary

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or appropriate to implement the provisions of this section consistent with the purposes of this section.”

(b) PROTECTION FOR EMPLOYEES OF NATIONALLY RECOGNIZED STATISTICAL RATING ORGANIZATIONS.—Section 1514A(a) of title 18, United States Code, is amended—

(1) by inserting “or nationally recognized statistical rating organization (as defined in section 3(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78c),” after “78o(d),”; and

(2) by inserting “or nationally recognized statistical rating organization” after “such company”.

(c) SECTION 1514A OF TITLE 18, UNITED STATES CODE.—

(1) STATUTE OF LIMITATIONS; JURY TRIAL.—Section 1514A(b)(2) of title 18, United States Code, is amended—

(A) in subparagraph (D)—

(i) by striking “90” and inserting “180”; and

(ii) by striking the period at the end and inserting “, or after the date on which the employee became aware of the violation.”; and

(B) by adding at the end the following:

“(E) JURY TRIAL.—A party to an action brought under paragraph (1)(B) shall be entitled to trial by jury.”.

(2) PRIVATE SECURITIES LITIGATION WITNESSES; NON-ENFORCEABILITY; INFORMATION.—Section 1514A of title 18, United States Code, is amended by adding at the end the following:

“(e) NONENFORCEABILITY OF CERTAIN PROVISIONS WAIVING RIGHTS AND REMEDIES OR REQUIRING ARBITRATION OF DISPUTES.—

“(1) WAIVER OF RIGHTS AND REMEDIES.—The rights and remedies provided for in this section may not be waived by any agreement, policy form, or condition of employment, including by a predispute arbitration agreement.

“(2) PREDISPUTE ARBITRATION AGREEMENTS.—No predispute arbitration agreement shall be valid or enforceable, if the agreement requires arbitration of a dispute arising under this section.”.

(d) STUDY OF WHISTLEBLOWER PROTECTION PROGRAM.—

(1) STUDY.—The Inspector General of the Commission shall conduct a study of the whistleblower protections established under the amendments made by this section, including—

(A) whether the final rules and regulation issued under the amendments made by this section have made the whistleblower protection program (referred to in this subsection as the “program”) clearly defined and user-friendly;

(B) whether the program is promoted on the website of the Commission and has been widely publicized;

(C) whether the Commission is prompt in—

(i) responding to—

(I) information provided by whistleblowers;

and

(II) applications for awards filed by whistleblowers;

(ii) updating whistleblowers about the status of their applications; and

(iii) otherwise communicating with the interested parties;

(D) whether the minimum and maximum reward levels are adequate to entice whistleblowers to come forward with

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information and whether the reward levels are so high as to encourage illegitimate whistleblower claims;

(E) whether the appeals process has been unduly burdensome for the Commission;

(F) whether the funding mechanism for the Investor Protection Fund is adequate;

(G) whether, in the interest of protecting investors and identifying and preventing fraud, it would be useful for Congress to consider empowering whistleblowers or other individuals, who have already attempted to pursue the case through the Commission, to have a private right of action to bring suit based on the facts of the same case, on behalf of the Government and themselves, against persons who have committed securities fraud;

(H)(i) whether the exemption under section 552(b)(3) of title 5 (known as the Freedom of Information Act) established in section 21F(h)(2)(A) of the Securities Exchange Act of 1934, as added by this Act, aids whistleblowers in disclosing information to the Commission;

(ii) what impact the exemption described in clause (i) has had on the ability of the public to access information about the regulation and enforcement by the Commission of securities; and

(iii) any recommendations on whether the exemption described in clause (i) should remain in effect; and

(I) such other matters as the Inspector General deems appropriate.

(2) REPORT.—Not later than 30 months after the date of enactment of this Act, the Inspector General shall—

(A) submit a report on the findings of the study required under paragraph (1) to the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on Financial Services of the House; and

(B) make the report described in subparagraph (A) available to the public through publication of the report on the website of the Commission.

SEC. 923. CONFORMING AMENDMENTS FOR WHISTLEBLOWER PROTECTION.

(a) IN GENERAL.—

(1) SECURITIES ACT OF 1933.—Section 20(d)(3)(A) of the Securities Act of 1933 (15 U.S.C. 77t(d)(3)(A)) is amended by inserting “and section 21F of the Securities Exchange Act of 1934” after “the Sarbanes-Oxley Act of 2002”.

(2) INVESTMENT COMPANY ACT OF 1940.—Section 42(e)(3)(A) of the Investment Company Act of 1940 (15 U.S.C. 80a-41(e)(3)(A)) is amended by inserting “and section 21F of the Securities Exchange Act of 1934” after “the Sarbanes-Oxley Act of 2002”.

(3) INVESTMENT ADVISERS ACT OF 1940.—Section 209(e)(3)(A) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-9(e)(3)(A)) is amended by inserting “and section 21F of the Securities Exchange Act of 1934” after “the Sarbanes-Oxley Act of 2002”.

(b) SECURITIES EXCHANGE ACT.—

(1) SECTION 21.—Section 21(d)(3)(C)(i) of the Securities Exchange Act of 1934 (15 U.S.C. 78u(d)(3)(C)(i)) is amended

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by inserting "and section 21F of this title" after "the Sarbanes-Oxley Act of 2002".

(2) SECTION 21A.—Section 21A of the Securities Exchange Act of 1934 (15 U.S.C. 78a-1) is amended—

(A) in subsection (d)(1) by—

(i) striking "(subject to subsection (e))"; and

(ii) inserting "and section 21F of this title" after "the Sarbanes-Oxley Act of 2002";

(B) by striking subsection (e); and

(C) by redesignating subsections (f) and (g) as subsections (e) and (f), respectively.

SEC. 924. IMPLEMENTATION AND TRANSITION PROVISIONS FOR WHISTLEBLOWER PROTECTION.

(a) **IMPLEMENTING RULES.**—The Commission shall issue final regulations implementing the provisions of section 21F of the Securities Exchange Act of 1934, as added by this subtitle, not later than 270 days after the date of enactment of this Act.

(b) **ORIGINAL INFORMATION.**—Information provided to the Commission in writing by a whistleblower shall not lose the status of original information (as defined in section 21F(a)(3) of the Securities Exchange Act of 1934, as added by this subtitle) solely because the whistleblower provided the information prior to the effective date of the regulations, if the information is provided by the whistleblower after the date of enactment of this subtitle.

(c) **AWARDS.**—A whistleblower may receive an award pursuant to section 21F of the Securities Exchange Act of 1934, as added by this subtitle, regardless of whether any violation of a provision of the securities laws, or a rule or regulation thereunder, underlying the judicial or administrative action upon which the award is based, occurred prior to the date of enactment of this subtitle.

(d) **ADMINISTRATION AND ENFORCEMENT.**—The Securities and Exchange Commission shall establish a separate office within the Commission to administer and enforce the provisions of section 21F of the Securities Exchange Act of 1934 (as add by section 922(a)). Such office shall report annually to the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on Financial Services of the House of Representatives on its activities, whistleblower complaints, and the response of the Commission to such complaints.

SEC. 925. COLLATERAL BARS.

(a) **SECURITIES EXCHANGE ACT OF 1934.**—

(1) **SECTION 15.**—Section 15(b)(6)(A) of the Securities Exchange Act of 1934 (15 U.S.C. 78o(b)(6)(A)) is amended by striking "12 months, or bar such person from being associated with a broker or dealer," and inserting "12 months, or bar any such person from being associated with a broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization."

(2) **SECTION 15B.**—Section 15B(c)(4) of the Securities Exchange Act of 1934 (15 U.S.C. 78o-4(c)(4)) is amended by striking "twelve months or bar any such person from being associated with a municipal securities dealer," and inserting "12 months or bar any such person from being associated with a broker, dealer, investment adviser, municipal securities

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SEC. 927. EQUAL TREATMENT OF SELF-REGULATORY ORGANIZATION RULES.

Section 29(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78cc(a)) is amended by striking "an exchange required thereby" and inserting "a self-regulatory organization."

SEC. 928. CLARIFICATION THAT SECTION 205 OF THE INVESTMENT ADVISERS ACT OF 1940 DOES NOT APPLY TO STATE-REGISTERED ADVISERS.

Section 205(a) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-5(a)) is amended, in the matter preceding paragraph (1)—

- (1) by striking ", unless exempt from registration pursuant to section 203(b)," and inserting "registered or required to be registered with the Commission";
- (2) by striking "make use of the mails or any means or instrumentality of interstate commerce, directly or indirectly, to"; and
- (3) by striking "to" after "in any way".

SEC. 929. UNLAWFUL MARGIN LENDING.

Section 7(c)(1)(A) of the Securities Exchange Act of 1934 (15 U.S.C. 78g(c)(1)(A)) is amended by striking "; and" and inserting "; or".

SEC. 929A. PROTECTION FOR EMPLOYEES OF SUBSIDIARIES AND AFFILIATES OF PUBLICLY TRADED COMPANIES.

Section 1514A of title 18, United States Code, is amended by inserting "including any subsidiary or affiliate whose financial information is included in the consolidated financial statements of such company" after "the Securities Exchange Act of 1934 (15 U.S.C. 78o(d))".

SEC. 929B. FAIR FUND AMENDMENTS.

Section 308 of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7246(a)) is amended—

- (1) by striking subsection (a) and inserting the following:

"(a) CIVIL PENALTIES TO BE USED FOR THE RELIEF OF VICTIMS.—If, in any judicial or administrative action brought by the Commission under the securities laws, the Commission obtains a civil penalty against any person for a violation of such laws, or such person agrees, in settlement of any such action, to such civil penalty, the amount of such civil penalty shall, on the motion or at the direction of the Commission, be added to and become part of a disgorgement fund or other fund established for the benefit of the victims of such violation.";
- (2) in subsection (b)—
 - (A) by striking "for a disgorgement fund described in subsection (a)" and inserting "for a disgorgement fund or other fund described in subsection (a)"; and
 - (B) by striking "in the disgorgement fund" and inserting "in such fund"; and
- (3) by striking subsection (e).

SEC. 929C. INCREASING THE BORROWING LIMIT ON TREASURY LOANS.

Section 4(h) of the Securities Investor Protection Act of 1970 (15 U.S.C. 78ddd(h)) is amended in the first sentence, by striking "\$1,000,000,000" and inserting "\$2,500,000,000".

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- (B) the gravity of the violation or failure to pay;
- (C) the severity of the risks to or losses of the consumer, which may take into account the number of products or services sold or provided;
- (D) the history of previous violations; and
- (E) such other matters as justice may require.

(4) **AUTHORITY TO MODIFY OR REMIT PENALTY.**—The Bureau may compromise, modify, or remit any penalty which may be assessed or had already been assessed under paragraph (2). The amount of such penalty, when finally determined, shall be exclusive of any sums owed by the person to the United States in connection with the costs of the proceeding, and may be deducted from any sums owing by the United States to the person charged.

(5) **NOTICE AND HEARING.**—No civil penalty may be assessed under this subsection with respect to a violation of any Federal consumer financial law, unless—

- (A) the Bureau gives notice and an opportunity for a hearing to the person accused of the violation; or
- (B) the appropriate court has ordered such assessment and entered judgment in favor of the Bureau.

SEC. 1056. REFERRALS FOR CRIMINAL PROCEEDINGS.

If the Bureau obtains evidence that any person, domestic or foreign, has engaged in conduct that may constitute a violation of Federal criminal law, the Bureau shall transmit such evidence to the Attorney General of the United States, who may institute criminal proceedings under appropriate law. Nothing in this section affects any other authority of the Bureau to disclose information.

SEC. 1057. EMPLOYEE PROTECTION.

(a) **IN GENERAL.**—No covered person or service provider shall terminate or in any other way discriminate against, or cause to be terminated or discriminated against, any covered employee or any authorized representative of covered employees by reason of the fact that such employee or representative, whether at the initiative of the employee or in the ordinary course of the duties of the employee (or any person acting pursuant to a request of the employee), has—

(1) provided, caused to be provided, or is about to provide or cause to be provided, information to the employer, the Bureau, or any other State, local, or Federal, government authority or law enforcement agency relating to any violation of, or any act or omission that the employee reasonably believes to be a violation of, any provision of this title or any other provision of law that is subject to the jurisdiction of the Bureau, or any rule, order, standard, or prohibition prescribed by the Bureau;

(2) testified or will testify in any proceeding resulting from the administration or enforcement of any provision of this title or any other provision of law that is subject to the jurisdiction of the Bureau, or any rule, order, standard, or prohibition prescribed by the Bureau;

(3) filed, instituted, or caused to be filed or instituted any proceeding under any Federal consumer financial law; or

(4) objected to, or refused to participate in, any activity, policy, practice, or assigned task that the employee (or other such person) reasonably believed to be in violation of any law,

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rule, order, standard, or prohibition, subject to the jurisdiction of, or enforceable by, the Bureau.

(b) **DEFINITION OF COVERED EMPLOYEE.**—For the purposes of this section, the term “covered employee” means any individual performing tasks related to the offering or provision of a consumer financial product or service.

(c) **PROCEDURES AND TIMETABLES.**—

(1) **COMPLAINT.**—

(A) **IN GENERAL.**—A person who believes that he or she has been discharged or otherwise discriminated against by any person in violation of subsection (a) may, not later than 180 days after the date on which such alleged violation occurs, file (or have any person file on his or her behalf) a complaint with the Secretary of Labor alleging such discharge or discrimination and identifying the person responsible for such act.

(B) **ACTIONS OF SECRETARY OF LABOR.**—Upon receipt of such a complaint, the Secretary of Labor shall notify, in writing, the person named in the complaint who is alleged to have committed the violation, of—

- (i) the filing of the complaint;
- (ii) the allegations contained in the complaint;
- (iii) the substance of evidence supporting the complaint; and
- (iv) opportunities that will be afforded to such person under paragraph (2).

(2) **INVESTIGATION BY SECRETARY OF LABOR.**—

(A) **IN GENERAL.**—Not later than 60 days after the date of receipt of a complaint filed under paragraph (1), and after affording the complainant and the person named in the complaint who is alleged to have committed the violation that is the basis for the complaint an opportunity to submit to the Secretary of Labor a written response to the complaint and an opportunity to meet with a representative of the Secretary of Labor to present statements from witnesses, the Secretary of Labor shall—

- (i) initiate an investigation and determine whether there is reasonable cause to believe that the complaint has merit; and
- (ii) notify the complainant and the person alleged to have committed the violation of subsection (a), in writing, of such determination.

(B) **NOTICE OF RELIEF AVAILABLE.**—If the Secretary of Labor concludes that there is reasonable cause to believe that a violation of subsection (a) has occurred, the Secretary of Labor shall, together with the notice under subparagraph (A)(ii), issue a preliminary order providing the relief prescribed by paragraph (4)(B).

(C) **REQUEST FOR HEARING.**—Not later than 30 days after the date of receipt of notification of a determination of the Secretary of Labor under this paragraph, either the person alleged to have committed the violation or the complainant may file objections to the findings or preliminary order, or both, and request a hearing on the record. The filing of such objections shall not operate to stay any reinstatement remedy contained in the preliminary order. Any such hearing shall be conducted expeditiously, and

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if a hearing is not requested in such 30-day period, the preliminary order shall be deemed a final order that is not subject to judicial review.

(3) GROUNDS FOR DETERMINATION OF COMPLAINTS.—

(A) IN GENERAL.—The Secretary of Labor shall dismiss a complaint filed under this subsection, and shall not conduct an investigation otherwise required under paragraph (2), unless the complainant makes a prima facie showing that any behavior described in paragraphs (1) through (4) of subsection (a) was a contributing factor in the unfavorable personnel action alleged in the complaint.

(B) REBUTTAL EVIDENCE.—Notwithstanding a finding by the Secretary of Labor that the complainant has made the showing required under subparagraph (A), no investigation otherwise required under paragraph (2) shall be conducted, if the employer demonstrates, by clear and convincing evidence, that the employer would have taken the same unfavorable personnel action in the absence of that behavior.

(C) EVIDENTIARY STANDARDS.—The Secretary of Labor may determine that a violation of subsection (a) has occurred only if the complainant demonstrates that any behavior described in paragraphs (1) through (4) of subsection (a) was a contributing factor in the unfavorable personnel action alleged in the complaint. Relief may not be ordered under subparagraph (A) if the employer demonstrates by clear and convincing evidence that the employer would have taken the same unfavorable personnel action in the absence of that behavior.

(4) ISSUANCE OF FINAL ORDERS; REVIEW PROCEDURES.—

(A) TIMING.—Not later than 120 days after the date of conclusion of any hearing under paragraph (2), the Secretary of Labor shall issue a final order providing the relief prescribed by this paragraph or denying the complaint. At any time before issuance of a final order, a proceeding under this subsection may be terminated on the basis of a settlement agreement entered into by the Secretary of Labor, the complainant, and the person alleged to have committed the violation.

(B) PENALTIES.—

(i) ORDER OF SECRETARY OF LABOR.—If, in response to a complaint filed under paragraph (1), the Secretary of Labor determines that a violation of subsection (a) has occurred, the Secretary of Labor shall order the person who committed such violation—

(I) to take affirmative action to abate the violation;

(II) to reinstate the complainant to his or her former position, together with compensation (including back pay) and restore the terms, conditions, and privileges associated with his or her employment; and

(III) to provide compensatory damages to the complainant.

(ii) PENALTY.—If an order is issued under clause (i), the Secretary of Labor, at the request of the complainant, shall assess against the person against

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whom the order is issued, a sum equal to the aggregate amount of all costs and expenses (including attorney fees and expert witness fees) reasonably incurred, as determined by the Secretary of Labor, by the complainant for, or in connection with, the bringing of the complaint upon which the order was issued.

(C) PENALTY FOR FRIVOLOUS CLAIMS.—If the Secretary of Labor finds that a complaint under paragraph (1) is frivolous or has been brought in bad faith, the Secretary of Labor may award to the prevailing employer a reasonable attorney fee, not exceeding \$1,000, to be paid by the complainant.

(D) DE NOVO REVIEW.—

(i) FAILURE OF THE SECRETARY TO ACT.—If the Secretary of Labor has not issued a final order within 210 days after the date of filing of a complaint under this subsection, or within 90 days after the date of receipt of a written determination, the complainant may bring an action at law or equity for de novo review in the appropriate district court of the United States having jurisdiction, which shall have jurisdiction over such an action without regard to the amount in controversy, and which action shall, at the request of either party to such action, be tried by the court with a jury.

(ii) PROCEDURES.—A proceeding under clause (i) shall be governed by the same legal burdens of proof specified in paragraph (3). The court shall have jurisdiction to grant all relief necessary to make the employee whole, including injunctive relief and compensatory damages, including—

(I) reinstatement with the same seniority status that the employee would have had, but for the discharge or discrimination;

(II) the amount of back pay, with interest;

and

(III) compensation for any special damages sustained as a result of the discharge or discrimination, including litigation costs, expert witness fees, and reasonable attorney fees.

(E) OTHER APPEALS.—Unless the complainant brings an action under subparagraph (D), any person adversely affected or aggrieved by a final order issued under subparagraph (A) may file a petition for review of the order in the United States Court of Appeals for the circuit in which the violation with respect to which the order was issued, allegedly occurred or the circuit in which the complainant resided on the date of such violation, not later than 60 days after the date of the issuance of the final order of the Secretary of Labor under subparagraph (A). Review shall conform to chapter 7 of title 5, United States Code. The commencement of proceedings under this subparagraph shall not, unless ordered by the court, operate as a stay of the order. An order of the Secretary of Labor with respect to which review could have been obtained under this subparagraph shall not be subject to judicial review in any criminal or other civil proceeding.

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(5) FAILURE TO COMPLY WITH ORDER.—

(A) ACTIONS BY THE SECRETARY.—If any person has failed to comply with a final order issued under paragraph (4), the Secretary of Labor may file a civil action in the United States district court for the district in which the violation was found to have occurred, or in the United States district court for the District of Columbia, to enforce such order. In actions brought under this paragraph, the district courts shall have jurisdiction to grant all appropriate relief including injunctive relief and compensatory damages.

(B) CIVIL ACTIONS TO COMPEL COMPLIANCE.—A person on whose behalf an order was issued under paragraph (4) may commence a civil action against the person to whom such order was issued to require compliance with such order. The appropriate United States district court shall have jurisdiction, without regard to the amount in controversy or the citizenship of the parties, to enforce such order.

(C) AWARD OF COSTS AUTHORIZED.—The court, in issuing any final order under this paragraph, may award costs of litigation (including reasonable attorney and expert witness fees) to any party, whenever the court determines such award is appropriate.

(D) MANDAMUS PROCEEDINGS.—Any nondiscretionary duty imposed by this section shall be enforceable in a mandamus proceeding brought under section 1361 of title 28, United States Code.

(d) UNENFORCEABILITY OF CERTAIN AGREEMENTS.—

(1) NO WAIVER OF RIGHTS AND REMEDIES.—Except as provided under paragraph (3), and notwithstanding any other provision of law, the rights and remedies provided for in this section may not be waived by any agreement, policy, form, or condition of employment, including by any predispute arbitration agreement.

(2) NO PREDISPUTE ARBITRATION AGREEMENTS.—Except as provided under paragraph (3), and notwithstanding any other provision of law, no predispute arbitration agreement shall be valid or enforceable to the extent that it requires arbitration of a dispute arising under this section.

(3) EXCEPTION.—Notwithstanding paragraphs (1) and (2), an arbitration provision in a collective bargaining agreement shall be enforceable as to disputes arising under subsection (a)(4), unless the Bureau determines, by rule, that such provision is inconsistent with the purposes of this title.

SEC. 1058. EFFECTIVE DATE.

This subtitle shall become effective on the designated transfer date.

Subtitle F—Transfer of Functions and Personnel; Transitional Provisions

SEC. 1061. TRANSFER OF CONSUMER FINANCIAL PROTECTION FUNCTIONS.

(a) DEFINED TERMS.—For purposes of this subtitle—

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SEC. 1079. REVIEW, REPORT, AND PROGRAM WITH RESPECT TO EXCHANGE FACILITATORS.

(a) **REVIEW.**—The Director shall review all Federal laws and regulations relating to the protection of consumers who use exchange facilitators for transactions primarily for personal, family, or household purposes.

(b) **REPORT.**—Not later than 1 year after the designated transfer date, the Director shall submit to Congress a report describing—

(1) recommendations for legislation to ensure the appropriate protection of consumers who use exchange facilitators for transactions primarily for personal, family, or household purposes;

(2) recommendations for updating the regulations of Federal departments and agencies to ensure the appropriate protection of such consumers; and

(3) recommendations for regulations to ensure the appropriate protection of such consumers.

(c) **PROGRAM.**—Not later than 2 years after the date of the submission of the report under subsection (b), the Bureau shall, consistent with subtitle B, propose regulations or otherwise establish a program to protect consumers who use exchange facilitators.

(d) **EXCHANGE FACILITATOR DEFINED.**—In this section, the term “exchange facilitator” means a person that—

(1) facilitates, for a fee, an exchange of like kind property by entering into an agreement with a taxpayer by which the exchange facilitator acquires from the taxpayer the contractual rights to sell the taxpayer's relinquished property and transfers a replacement property to the taxpayer as a qualified intermediary (within the meaning of Treasury Regulations section 1.1031(k)-1(g)(4)) or enters into an agreement with the taxpayer to take title to a property as an exchange accommodation titleholder (within the meaning of Revenue Procedure 2000-37) or enters into an agreement with a taxpayer to act as a qualified trustee or qualified escrow holder (within the meaning of Treasury Regulations section 1.1031(k)-1(g)(3));

(2) maintains an office for the purpose of soliciting business to perform the services described in paragraph (1); or

(3) advertises any of the services described in paragraph (1) or solicits clients in printed publications, direct mail, television or radio advertisements, telephone calls, facsimile transmissions, or other electronic communications directed to the general public for purposes of providing any such services.

SEC. 1079A. FINANCIAL FRAUD PROVISIONS.

(a) **SENTENCING GUIDELINES.**—

(1) **SECURITIES FRAUD.**—

(A) **DIRECTIVE.**—Pursuant to its authority under section 994 of title 28, United States Code, and in accordance with this paragraph, the United States Sentencing Commission shall review and, if appropriate, amend the Federal Sentencing Guidelines and policy statements applicable to persons convicted of offenses relating to securities fraud or any other similar provision of law, in order to reflect the intent of Congress that penalties for the offenses under the guidelines and policy statements appropriately account for the potential and actual harm to the public and the financial markets from the offenses.

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(B) REQUIREMENTS.—In making any amendments to the Federal Sentencing Guidelines and policy statements under subparagraph (A), the United States Sentencing Commission shall—

(i) ensure that the guidelines and policy statements, particularly section 2B1.1(b)(14) and section 2B1.1(b)(17) (and any successors thereto), reflect—

(I) the serious nature of the offenses described in subparagraph (A);

(II) the need for an effective deterrent and appropriate punishment to prevent the offenses; and

(III) the effectiveness of incarceration in furthering the objectives described in subclauses (I) and (II);

(ii) consider the extent to which the guidelines appropriately account for the potential and actual harm to the public and the financial markets resulting from the offenses;

(iii) ensure reasonable consistency with other relevant directives and guidelines and Federal statutes;

(iv) make any necessary conforming changes to guidelines; and

(v) ensure that the guidelines adequately meet the purposes of sentencing, as set forth in section 3553(a)(2) of title 18, United States Code.

(2) FINANCIAL INSTITUTION FRAUD.—

(A) DIRECTIVE.—Pursuant to its authority under section 994 of title 28, United States Code, and in accordance with this paragraph, the United States Sentencing Commission shall review and, if appropriate, amend the Federal Sentencing Guidelines and policy statements applicable to persons convicted of fraud offenses relating to financial institutions or federally related mortgage loans and any other similar provisions of law, to reflect the intent of Congress that the penalties for the offenses under the guidelines and policy statements ensure appropriate terms of imprisonment for offenders involved in substantial bank frauds or other frauds relating to financial institutions.

(B) REQUIREMENTS.—In making any amendments to the Federal Sentencing Guidelines and policy statements under subparagraph (A), the United States Sentencing Commission shall—

(i) ensure that the guidelines and policy statements reflect—

(I) the serious nature of the offenses described in subparagraph (A);

(II) the need for an effective deterrent and appropriate punishment to prevent the offenses; and

(III) the effectiveness of incarceration in furthering the objectives described in subclauses (I) and (II);

(ii) consider the extent to which the guidelines appropriately account for the potential and actual harm

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to the public and the financial markets resulting from the offenses;

(iii) ensure reasonable consistency with other relevant directives and guidelines and Federal statutes;

(iv) make any necessary conforming changes to guidelines; and

(v) ensure that the guidelines adequately meet the purposes of sentencing, as set forth in section 3553(a)(2) of title 18, United States Code.

(b) EXTENSION OF STATUTE OF LIMITATIONS FOR SECURITIES FRAUD VIOLATIONS.—

(1) IN GENERAL.—Chapter 213 of title 18, United States Code, is amended by adding at the end the following:

“§ 3301. Securities fraud offenses

“(a) DEFINITION.—In this section, the term ‘securities fraud offense’ means a violation of, or a conspiracy or an attempt to violate—

“(1) section 1348;

“(2) section 32(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78ff(a));

“(3) section 24 of the Securities Act of 1933 (15 U.S.C. 77x);

“(4) section 217 of the Investment Advisers Act of 1940 (15 U.S.C. 80b-17);

“(5) section 49 of the Investment Company Act of 1940 (15 U.S.C. 80a-48); or

“(6) section 325 of the Trust Indenture Act of 1939 (15 U.S.C. 77yyy).

“(b) LIMITATION.—No person shall be prosecuted, tried, or punished for a securities fraud offense, unless the indictment is found or the information is instituted within 6 years after the commission of the offense.”

(2) TECHNICAL AND CONFORMING AMENDMENT.—The table of sections for chapter 213 of title 18, United States Code, is amended by adding at the end the following:

“3301. Securities fraud offenses.”

(c) AMENDMENTS TO THE FALSE CLAIMS ACT RELATING TO LIMITATIONS ON ACTIONS.—Section 3730(h) of title 31, United States Code, is amended—

(1) in paragraph (1), by striking “or agent on behalf of the employee, contractor, or agent or associated others in furtherance of other efforts to stop 1 or more violations of this subchapter” and inserting “agent or associated others in furtherance of an action under this section or other efforts to stop 1 or more violations of this subchapter”; and

(2) by adding at the end the following:

“(3) LIMITATION ON BRINGING CIVIL ACTION.—A civil action under this subsection may not be brought more than 3 years after the date when the retaliation occurred.”

Appendix G

SECURITIES AND EXCHANGE COMMISSION

17 CFR PART 202

[Release No. 34-61340]

Policy Statement Concerning Cooperation by Individuals in its Investigations and Related Enforcement Actions**AGENCY:** Securities and Exchange Commission.**ACTION:** Policy statement.**SUMMARY:** The Securities and Exchange Commission is issuing a policy statement announcing the analytical framework it uses to evaluate cooperation by individuals.**EFFECTIVE DATE:** January 19, 2010.**FOR FURTHER INFORMATION CONTACT:** Joan McKown, Chief Counsel, (202) 551-4933; or Jordan A. Thomas, Assistant Chief Litigation Counsel, (202) 551-4475.**SUPPLEMENTARY INFORMATION:**

The Securities and Exchange Commission is issuing a policy statement announcing the analytical framework it uses to evaluate cooperation by individuals. This framework serves two important purposes: it promotes the fair and effective exercise of discretion by the Commission, and it enhances confidence on the part of the public and cooperating individuals that decisions regarding cooperation in the Commission's investigations and related enforcement actions will be made in an appropriate and consistent manner.

The provisions of the Administrative Procedure Act ("APA"), 5 U.S.C. 553, regarding notice of proposed rulemaking, opportunities for public comment, and prior publication are not applicable to general statements of policy, such as this policy

statement. Similarly, the provisions of the Regulatory Flexibility Act, 5 U.S.C. 601-602, apply only when notice and comment are required by the APA or another statute and are therefore not applicable.

LIST OF SUBJECTS IN 17 CFR PART 202

Administrative practice and procedure.

TEXT OF AMENDMENT:

For the reasons set out in the preamble, Title 17, Chapter II of the Code of Federal Regulations is amended as follows:

PART 202—INFORMAL AND OTHER PROCEDURES

1. The authority citation for Part 202 continues to read, in part, as follows:

Authority: 15 U.S.C. 77s, 77t, 77sss, 77uuu, 78d-1, 78u, 78w, 78ll(d), 80a-37, 80a-41, 80b-9, 80b-11, 7202 and 7211 et seq., unless otherwise noted.

* * * * *

2. Add § 202.12 to read as follows:

§ 202.12 Policy statement concerning cooperation by individuals in its investigations and related enforcement actions.

Cooperation by individuals and entities in the Commission's investigations and related enforcement actions can contribute significantly to the success of the agency's mission. Cooperation can enhance the Commission's ability to detect violations of the federal securities laws, increase the effectiveness and efficiency of the Commission's investigations, and provide important evidence for the Commission's enforcement actions. There is a wide spectrum of tools available to the Commission and its staff for facilitating and rewarding cooperation by individuals, ranging from taking no enforcement action to pursuing reduced charges and sanctions in connection with

enforcement actions. As with any cooperation program, there exists some tension between the objectives of holding individuals fully accountable for their misconduct and providing incentives for individuals to cooperate with law enforcement authorities. This policy statement sets forth the analytical framework employed by the Commission and its staff for resolving this tension in a manner that ensures that potential cooperation arrangements maximize the Commission's law enforcement interests. Although the evaluation of cooperation requires a case-by-case analysis of the specific circumstances presented, as described in greater detail below, the Commission's general approach is to determine whether, how much, and in what manner to credit cooperation by individuals by evaluating four considerations: the assistance provided by the cooperating individual in the Commission's investigation or related enforcement actions ("Investigation"); the importance of the underlying matter in which the individual cooperated; the societal interest in ensuring that the cooperating individual is held accountable for his or her misconduct; and the appropriateness of cooperation credit based upon the profile of the cooperating individual. In the end, the goal of the Commission's analysis is to protect the investing public by determining whether the public interest in facilitating and rewarding an individual's cooperation in order to advance the Commission's law enforcement interests justifies the credit awarded to the individual for his or her cooperation.

(a) Assistance provided by the individual. The Commission assesses the assistance provided by the cooperating individual in the Investigation by considering, among other things:

(1) The value of the individual's cooperation to the Investigation including, but not limited to:

(i) Whether the individual's cooperation resulted in substantial assistance to the Investigation;

(ii) The timeliness of the individual's cooperation, including whether the individual was first to report the misconduct to the Commission or to offer his or her cooperation in the Investigation, and whether the cooperation was provided before he or she had any knowledge of a pending investigation or related action;

(iii) Whether the Investigation was initiated based on information or other cooperation provided by the individual;

(iv) The quality of cooperation provided by the individual, including whether the cooperation was truthful, complete, and reliable; and

(v) The time and resources conserved as a result of the individual's cooperation in the Investigation.

(2) The nature of the individual's cooperation in the Investigation including, but not limited to:

(i) Whether the individual's cooperation was voluntary or required by the terms of an agreement with another law enforcement or regulatory organization;

(ii) The types of assistance the individual provided to the Commission;

(iii) Whether the individual provided non-privileged information, which information was not requested by the staff or otherwise might not have been discovered;

(iv) Whether the individual encouraged or authorized others to assist the staff who might not have otherwise participated in the Investigation; and

(v) Any unique circumstances in which the individual provided the cooperation.

(b) Importance of the underlying matter. The Commission assesses the importance of the Investigation in which the individual cooperated by considering, among other things:

- (1) The character of the Investigation including, but not limited to:
 - (i) Whether the subject matter of the Investigation is a Commission priority;
 - (ii) The type of securities violations;
 - (iii) The age and duration of the misconduct;
 - (iv) The number of violations; and
 - (v) The isolated or repetitive nature of the violations.
- (2) The dangers to investors or others presented by the underlying violations

involved in the Investigation including, but not limited to:

- (i) The amount of harm or potential harm caused by the underlying violations;
- (ii) The type of harm resulting from or threatened by the underlying violations; and
- (iii) The number of individuals or entities harmed.¹

(c) Interest in holding the individual accountable. The Commission assesses the societal interest in holding the cooperating individual fully accountable for his or her misconduct by considering, among other things:

- (1) The severity of the individual's misconduct assessed by the nature of the violations and in the context of the individual's knowledge, education, training, experience, and position of responsibility at the time the violations occurred;

¹ Cooperation in Investigations that involve priority matters or serious, ongoing, or widespread violations will be viewed most favorably.

(2) The culpability of the individual, including, but not limited to, whether the individual acted with scienter, both generally and in relation to others who participated in the misconduct;

(3) The degree to which the individual tolerated illegal activity including, but not limited to, whether he or she took steps to prevent the violations from occurring or continuing, such as notifying the Commission or other appropriate law enforcement agency of the misconduct or, in the case of a violation involving a business organization, by notifying members of management not involved in the misconduct, the board of directors or the equivalent body not involved in the misconduct, or the auditors of such business organization of the misconduct;

(4) The efforts undertaken by the individual to remediate the harm caused by the violations including, but not limited to, whether he or she paid or agreed to pay disgorgement to injured investors and other victims or assisted these victims and the authorities in the recovery of the fruits and instrumentalities of the violations; and

(5) The sanctions imposed on the individual by other federal or state authorities and industry organizations for the violations involved in the Investigation.

(d) Profile of the individual. The Commission assesses whether, how much, and in what manner it is in the public interest to award credit for cooperation, in part, based upon the cooperating individual's personal and professional profile by considering, among other things:

(1) The individual's history of lawfulness, including complying with securities laws or regulations;

(2) The degree to which the individual has demonstrated an acceptance of responsibility for his or her past misconduct; and

(3) The degree to which the individual will have an opportunity to commit future violations of the federal securities laws in light of his or her occupation -- including, but not limited to, whether he or she serves as: a licensed individual, such as an attorney or accountant; an associated person of a regulated entity, such as a broker or dealer; a fiduciary for other individuals or entities regarding financial matters; an officer or director of public companies; or a member of senior management -- together with any existing or proposed safeguards based upon the individual's particular circumstances.

Note to § 202.12. Before the Commission evaluates an individual's cooperation, it analyzes the unique facts and circumstances of the case. The above principles are not listed in order of importance nor are they intended to be all-inclusive or to require a specific determination in any particular case. Furthermore, depending upon the facts and circumstances of each case, some of the principles may not be applicable or may deserve greater weight than others. Finally, neither this statement, nor the principles set forth herein creates or recognizes any legally enforceable rights for any person.

By the Commission.

Elizabeth M. Murphy
Secretary

Date: January 13, 2010

Appendix H

Securities and Exchange Commission
Division of Enforcement



Enforcement Manual

Office of Chief Counsel

*January 13, 2010**

** Includes conforming revisions as of March 3, 2010.*

6. Fostering Cooperation

The staff should carefully consider the use of cooperation by individuals and companies to advance its investigations and related enforcement actions.

6.1. Initial Considerations

6.1.1. Framework for Evaluating Cooperation by Individuals

17 CFR § 202.12 Policy Statement of the Securities and Exchange Commission Concerning Cooperation by Individuals in its Investigations and Related Enforcement Actions.

Cooperation by individuals and entities in the Commission's investigations and related enforcement actions can contribute significantly to the success of the agency's mission. Cooperation can enhance the Commission's ability to detect violations of the federal securities laws, increase the effectiveness and efficiency of the Commission's investigations, and provide important evidence for the Commission's enforcement actions. There is a wide spectrum of tools available to the Commission and its staff for facilitating and rewarding cooperation by individuals, ranging from taking no enforcement action to pursuing reduced charges and sanctions in connection with enforcement actions. As with any cooperation program, there exists some tension between the objectives of holding individuals fully accountable for their misconduct and providing incentives for individuals to cooperate with law enforcement authorities. This policy statement sets forth the analytical framework employed by the Commission and its staff for resolving this tension in a manner that ensures that potential cooperation arrangements maximize the Commission's law enforcement interests. Although the evaluation of cooperation requires a case-by-case analysis of the specific circumstances presented, as described in greater detail below, the Commission's general approach is to determine whether, how much, and in what manner to credit cooperation by individuals by evaluating four considerations: the assistance provided by the cooperating individual in the Commission's investigation or related enforcement actions ("Investigation"); the importance of the underlying matter in which the individual cooperated; the societal interest in ensuring that the cooperating individual is held accountable for his or her misconduct; and the appropriateness of cooperation credit based upon the profile of the cooperating individual. In the end, the goal of the Commission's analysis is to protect the investing public by determining whether the public interest in facilitating and rewarding

an individual's cooperation in order to advance the Commission's law enforcement interests justifies the credit awarded to the individual for his or her cooperation.

- (a) Assistance provided by the individual. The Commission assesses the assistance provided by the cooperating individual in the Investigation by considering, among other things:
- (1) The value of the individual's cooperation to the Investigation including, but not limited to:
 - (i) Whether the individual's cooperation resulted in substantial assistance to the Investigation;
 - (ii) The timeliness of the individual's cooperation, including whether the individual was first to report the misconduct to the Commission or to offer his or her cooperation in the Investigation, and whether the cooperation was provided before he or she had any knowledge of a pending investigation or related action;
 - (iii) Whether the Investigation was initiated based on information or other cooperation provided by the individual;
 - (iv) The quality of cooperation provided by the individual, including whether the cooperation was truthful, complete, and reliable; and
 - (v) The time and resources conserved as a result of the individual's cooperation in the Investigation.
 - (2) The nature of the individual's cooperation in the Investigation including, but not limited to:
 - (i) Whether the individual's cooperation was voluntary or required by the terms of an agreement with another law enforcement or regulatory organization;
 - (ii) The types of assistance the individual provided to the Commission;
 - (ii) Whether the individual provided non-privileged information, which information was not requested by the staff or otherwise might not have been discovered;

- (iv) Whether the individual encouraged or authorized others to assist the staff who might not have otherwise participated in the Investigation; and
 - (v) Any unique circumstances in which the individual provided the cooperation.
- (b) Importance of the underlying matter. The Commission assesses the importance of the Investigation in which the individual cooperated by considering, among other things:
- (1) The character of the Investigation including, but not limited to:
 - (i) Whether the subject matter of the Investigation is a Commission priority;
 - (ii) The type of securities violations;
 - (iii) The age and duration of the misconduct;
 - (iv) The number of violations; and
 - (v) The isolated or repetitive nature of the violations.
 - (2) The dangers to investors or others presented by the underlying violations involved in the Investigation including, but not limited to:
 - (i) The amount of harm or potential harm caused by the underlying violations;
 - (ii) The type of harm resulting from or threatened by the underlying violations; and
 - (iii) The number of individuals or entities harmed.⁸
- (c) Interest in holding the individual accountable. The Commission assesses the societal interest in holding the cooperating individual fully accountable for his or her misconduct by considering, among other things:
- (1) The severity of the individual's misconduct assessed by the nature of the violations and in the context of the individual's knowledge,

⁸ Cooperation in Investigations that involve priority matters or serious, ongoing, or widespread violations will be viewed most favorably.

- education, training, experience, and position of responsibility at the time the violations occurred;
- (2) The culpability of the individual, including, but not limited to, whether the individual acted with scienter, both generally and in relation to others who participated in the misconduct;
 - (3) The degree to which the individual tolerated illegal activity including, but not limited to, whether he or she took steps to prevent the violations from occurring or continuing, such as notifying the Commission or other appropriate law enforcement agency of the misconduct or, in the case of a violation involving a business organization, by notifying members of management not involved in the misconduct, the board of directors or the equivalent body not involved in the misconduct, or the auditors of such business organization of the misconduct;
 - (4) The efforts undertaken by the individual to remediate the harm caused by the violations including, but not limited to, whether he or she paid or agreed to pay disgorgement to injured investors and other victims or assisted these victims and the authorities in the recovery of the fruits and instrumentalities of the violations; and
 - (5) The sanctions imposed on the individual by other federal or state authorities and industry organizations for the violations involved in the Investigation.
- (d) Profile of the individual. The Commission assesses whether, how much, and in what manner it is in the public interest to award credit for cooperation, in part, based upon the cooperating individual's personal and professional profile by considering, among other things:
- (1) The individual's history of lawfulness, including complying with securities laws or regulations;
 - (2) The degree to which the individual has demonstrated an acceptance of responsibility for his or her past misconduct; and
 - (3) The degree to which the individual will have an opportunity to commit future violations of the federal securities laws in light of his or her occupation -- including, but not limited to, whether he or she serves as: a licensed individual, such as an attorney or accountant; an associated person of a regulated entity, such as a broker or dealer; a fiduciary for other individuals or entities regarding financial matters; an officer or director of public companies; or a member of senior management -- together with

any existing or proposed safeguards based upon the individual's particular circumstances.

Note to § 202.12. Before the Commission evaluates an individual's cooperation, it analyzes the unique facts and circumstances of the case. The above principles are not listed in order of importance nor are they intended to be all-inclusive or to require a specific determination in any particular case. Furthermore, depending upon the facts and circumstances of each case, some of the principles may not be applicable or may deserve greater weight than others. Finally, neither this statement, nor the principles set forth herein creates or recognizes any legally enforceable rights for any person.

6.1.2. Framework for Evaluating Cooperation by Companies

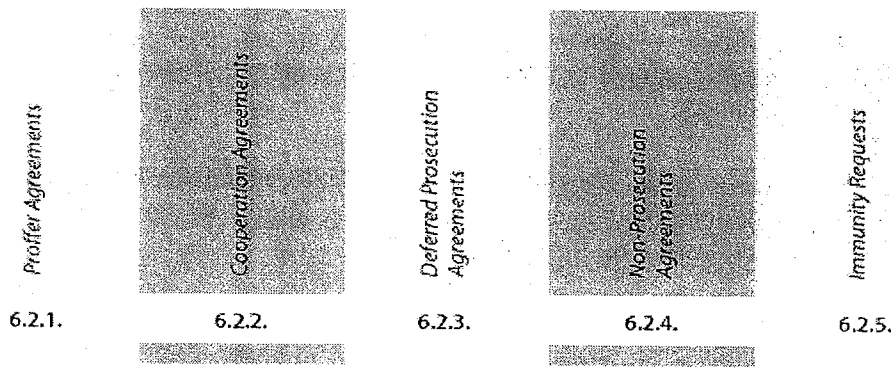
In October 2001, the Commission issued a Report of Investigation and Statement explaining its decision not to take enforcement action against a public company it had investigated for financial statement irregularities. *Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934 and Commission Statement on the Relationship of Cooperation to Agency Enforcement Decisions*, SEC Rel. Nos. 34-44969 and AAER-1470 (Oct. 23, 2001) (<http://www.sec.gov/litigation/investreport/34-44969.htm>.) In this report, commonly referred to as the Seaboard Report, the Commission articulated an analytical framework for evaluating cooperation by companies. The report detailed the many factors the Commission considers in determining whether, and to what extent, it grants leniency to investigated companies for cooperating in its investigations and for related good corporate citizenship. Specifically, the report identifies four broad measures of a company's cooperation:

- Self-policing prior to the discovery of the misconduct, including establishing effective compliance procedures and an appropriate tone at the top;
- Self-reporting of misconduct when it is discovered, including conducting a thorough review of the nature, extent, origins and consequences of the misconduct, and promptly, completely and effectively disclosing the misconduct to the public, to regulatory agencies, and to self-regulatory organizations;
- Remediation, including dismissing or appropriately disciplining wrongdoers, modifying and improving internal controls and procedures to prevent recurrence of the misconduct, and appropriately compensating those adversely affected; and
- Cooperation with law enforcement authorities, including providing the Commission staff with all information relevant to the underlying violations and the company's remedial efforts.

Since every enforcement matter is different, this analytical framework sets forth general principles but does not limit the Commission's broad discretion to evaluate every case individually, on its own unique facts and circumstances. Similar to the Commission's treatment of cooperating individuals, credit for cooperation by companies may range from taking no enforcement action to pursuing reduced charges and sanctions in connection with enforcement actions. For greater detail regarding the analytical framework used by the Commission to evaluate cooperation by companies, the staff should review the Seaboard Report (<http://www.sec.gov/litigation/investreport/34-44969.htm>).

6.2. Cooperation Tools

There is a wide spectrum of tools available to the staff for facilitating and rewarding cooperation in its investigations and related enforcement actions. A non-exclusive list of cooperation tools appears below. Since every enforcement matter is unique, the appropriate use of a cooperation tool invariably depends upon a careful analysis of the facts and circumstances of each case. In some cases, multiple cooperation tools may be appropriate.



6.2.1. Proffer Agreements

Introduction:

Proffers by attorneys and cooperating individuals are an important vehicle used by the staff to assess the probable value of cooperation by individuals and companies and for those individuals and companies to initiate discussions regarding the benefits that may be available if they cooperate. Proffer agreements are regularly used by the staff to facilitate proffer sessions.

Basics:

A proffer agreement is a written agreement providing that any statements made by a person, on a specific date, may not be used against that individual in subsequent proceedings, except that the Commission may use statements made during the proffer session as a source of leads to discover additional evidence and for impeachment or

rebuttal purposes if the person testifies or argues inconsistently in a subsequent proceeding. The Commission also may share the information provided by the proffering individual with appropriate authorities in a prosecution for perjury, making a false statement or obstruction of justice.

Procedures:

Proffer agreements must be signed by a supervisor at or above the level of Assistant Director.

Considerations:

- In most cases, the staff should require a potential cooperating individual to make a detailed proffer before selecting and utilizing other cooperation tools.
- The Commission may use information provided at a proffer session to advance its investigation or to generate leads to new evidence that the staff might not otherwise have discovered.
- To avoid potential misunderstandings regarding the nature of proffer sessions, with few exceptions, proffer sessions should be conducted pursuant to written proffer agreements.
- The staff uses a standard proffer agreement. Modifications to the standard agreement should not be made without first consulting with staff in the Office of Chief Counsel or the Chief Litigation Counsel.
- If the staff conducts a joint proffer session with criminal authorities, the staff should address any potential substantive or procedural issues with his or her supervisors, as well as the Assistant United States Attorney or state prosecutor on the case, before the proffer begins. In cases where the staff participates in a proffer with the criminal authorities and the cooperating individual has not asked for a proffer letter from the Commission, the staff should remind the individual that the proffer agreement with the criminal authorities does not apply to the Commission.

Related Tool:

- Oral Assurances—Where the available evidence indicates that an individual or company has not violated the federal securities laws such as to warrant an enforcement action, Assistant Directors, with the approval of a supervisor at or above the level of Associate Director, may orally inform the individual or company that the Division does not anticipate recommending an enforcement action against the individual or company based upon the evidence currently known to the staff.

- Oral assurances are only authorized when the investigative record is adequately developed. Accordingly, prior to providing an oral assurance, the staff should preferably receive proffers from the potential cooperating individuals and companies or have sufficient information regarding the potential cooperators' conduct and their ability to provide substantial assistance to the Commission's investigations or related enforcement actions.
- Whenever oral assurances are provided, the staff should clearly inform the potential cooperating individual or company that oral assurances are based upon the evidence currently known to the staff, the Division's enforcement recommendations may change if new evidence is subsequently discovered and that the Commission has final authority to accept or reject enforcement recommendations.
- After an oral assurance has been provided, the staff should contemporaneously prepare and retain a brief memorandum to file summarizing the assurance provided.

6.2.2. Cooperation Agreements

Basics:

A cooperation agreement is a written agreement between the Division of Enforcement and a potential cooperating individual or company prepared to provide substantial assistance to the Commission's investigation and related enforcement actions. Specifically, in a cooperation agreement, the Division agrees to recommend to the Commission that the individual or company receive credit for cooperating in its investigation and related enforcement actions and, under certain circumstances, to make specific enforcement recommendations if, among other things: 1) the Division concludes that the individual or company has provided or is likely to provide substantial assistance to the Commission; 2) the individual or company agrees to cooperate truthfully and fully in the Commission's investigation and related enforcement actions and waive the applicable statute of limitations; and 3) the individual or company satisfies his/her/its obligations under the agreement. If the agreement is violated, the staff may recommend an enforcement action to the Commission against the individual or company without any limitation.

Procedures:

- Prior to seeking authority to enter into cooperation agreements, the staff should preferably receive proffers from the potential cooperating individuals and companies or have sufficient information regarding their ability to provide substantial assistance to the Commission's investigations or related enforcement actions.

- The Director and those senior officers designated by the Director have the authority to enter into cooperation agreements on behalf of the Division.
- The staff should prepare a contemporaneous memorandum to the file documenting the basis for entering into the cooperation agreement. This memorandum, along with a copy of the executed agreement, should be maintained by the senior officer who executed the agreement.

Considerations:

- In addition to the standard cooperation analysis set forth in Section 6.1 of the Manual, when assessing whether to recommend that the Division enter into a cooperation agreement with an individual or company, the staff should consider:
 - whether other means of obtaining the desired cooperation are available and likely to be timely and effective; and
 - whether the individual or company has entered into or is likely to enter into a plea agreement with criminal prosecutors that will require the individual or company to cooperate in the Commission's investigation and related enforcement actions.
- The staff should advise potential cooperating individuals or companies that cooperation agreements entered into with the Division do not bind the Commission and that the Division cannot, and does not, make any promise or representation as to whether or how the Commission may act on enforcement recommendations made by the Division.
- Cooperation agreements should generally include the following terms:
 - the cooperating individual or company agrees to cooperate truthfully and fully, as directed by the Division's staff, in investigations and related enforcement proceedings including, but not limited to, producing all potentially relevant non-privileged documents and materials to the Commission, responding to all inquiries, appearing for interviews, and testifying at trials and other judicial proceedings as requested by the staff, and waiving the territorial limits on service contained in Rule 45 of the Federal Rules of Civil Procedure;
 - the cooperating individual or company agrees to waive the applicable statute of limitations period;
 - the cooperating individual or company agrees not to violate the securities laws;
 - the cooperating individual or company acknowledges that the agreement does not constitute a final disposition of any potential enforcement action;

- the Division will bring the assistance provided by the cooperating individual or company to the attention of the Commission and other regulatory and law enforcement authorities requested by the cooperating individual or company; and
- the cooperating individual or company acknowledges that, although the Division has discretion to make enforcement recommendations, only the Commission has the authority to approve enforcement dispositions and accept settlement offers.
- If the Division agrees to make a specific enforcement recommendation to the Commission, the staff should consider the settlement terms of other similar cases to identify prior precedent involving similar alleged misconduct and include the following terms in the cooperation agreement:
 - the federal securities laws alleged to have been violated;
 - the cooperating individual or company agrees to resolve the matter without admitting or denying the alleged violations;
 - the specific enforcement recommendation the Division expects to make if the cooperating individual or company satisfies the terms of the agreement; and
 - any agreement to make a specific enforcement recommendation to the Commission shall be conditioned upon the Division's assessment that the cooperating individual or company has rendered substantial assistance in a Commission investigation or related enforcement action.
- The Division uses a standard form of cooperation agreement to be adapted to the specific circumstances of the investigation or related enforcement action.

Related Tools:

- Settlement Recommendations—Even in the absence of a cooperation agreement, the staff may take into account an individual or company's cooperation in connection with recommending sanctions or charges associated with the alleged misconduct and, under certain circumstances, forgoing enforcement actions against a cooperating individual or company.
 - To determine whether, how much, and in what manner to recommend cooperation credit, the staff should consider the settlement terms of other similar cases to identify prior precedent involving similar alleged misconduct and apply the factors outlined in Section 6.1 of the Manual.

- Where cooperation credit is being recommended to or has been authorized by the Commission in settlements, the staff should include standard language relating to cooperation in the related Offers or Consents, unless such disclosure would not advance the goals of the Commission's cooperation program or would adversely affect related ongoing investigations or proceedings. Modifications to this standard language should not be made without first consulting with staff in the Office of Chief Counsel or the Chief Litigation Counsel.
- Where cooperation language is included in settlement papers, the staff generally should include a reference to the individual or company's cooperation in the Commission's related litigation and/or press releases.
- Cooperation Letters—Upon the written request of cooperating individuals and companies, supervisors at or above the level of Associate Director may submit letters describing the fact, manner and extent of assistance provided by such cooperating individuals and companies to the attention of courts, regulatory organizations, or law enforcement authorities. Requests for cooperation letters and copies of the letters sent by Commission staff should be retained by the senior officers who sign them.

Further information:

- For assistance in drafting cooperation agreements, please consult with staff in the Office of the Chief Counsel or the Chief Litigation Counsel.

6.2.3. Deferred Prosecution Agreements

Basics:

A deferred prosecution agreement is a written agreement between the Commission and a potential cooperating individual or company in which the Commission agrees to forego an enforcement action against the individual or company if the individual or company agrees to, among other things: 1) cooperate truthfully and fully in the Commission's investigation and related enforcement actions; 2) enter into a long-term tolling agreement; 3) comply with express prohibitions and/or undertakings during a period of deferred prosecution; and 4) under certain circumstances, agree either to admit or not to contest underlying facts that the Commission could assert to establish a violation of the federal securities laws. If the agreement is violated during the period of deferred prosecution, the staff may recommend an enforcement action to the Commission against the individual or company without limitation for the original misconduct as well as any additional misconduct. Furthermore, if the Commission authorizes the enforcement action, the staff may use any factual admissions made by the cooperating individual or company to file a motion for summary judgment, while maintaining the ability to bring an enforcement action for any additional misconduct at a later date.

Procedures:

- Prior to seeking authority to enter into a deferred prosecution agreement, the staff should receive proffers from the cooperating individual and/or company.
- Deferred prosecution agreements must be approved by the Commission.
- Unless the Commission directs otherwise, deferred prosecution agreements will be made available to the public upon request.

Considerations:

- To determine whether to recommend that the Commission enter into a deferred prosecution agreement, the staff should use the standard cooperation analysis set forth in Section 6.1 of the Manual.
- An admission or an agreement not to contest the relevant facts underlying the alleged offenses generally is appropriate and should be carefully considered for the following:
 - licensed individuals, such as attorneys and accountants;
 - regulated individuals, such as registered brokers or dealers;
 - fiduciaries for other individuals or entities regarding financial matters;
 - officers and directors of public companies; and
 - individuals or companies with a prior history of violating the securities laws.
- A deferred prosecution agreement should generally include the following terms:
 - the cooperating individual or company agrees to cooperate truthfully and fully, as directed by the Division's staff, in investigations and related enforcement proceedings including, but not limited to, producing all potentially relevant non-privileged documents and materials to the Commission, responding to all inquiries, appearing for interviews, and testifying at trials and other judicial proceedings as requested by the staff, and waiving the territorial limits on service contained in Rule 45 of the Federal Rules of Civil Procedure;
 - the cooperating individual or company agrees to toll the applicable statute of limitations period;

- the cooperating individual or company agrees not to violate the securities laws;
 - the cooperating individual or company shall make any agreed upon disgorgement or penalty payments;
 - if the cooperating individual or company satisfies the terms of the deferred prosecution agreement during the term of the agreement, the Commission will not pursue any further enforcement action concerning the matter referenced in the agreement;
 - if the individual or company violates the agreement during its term, the Division may recommend and the Commission may pursue an enforcement action against the individual or company without limitation;
 - the cooperating individual or company agrees that the Commission may use statements, information, and materials provided pursuant to the agreement against him/her/it if the individual or company violates the terms of the agreement; and
 - additional prohibitions and undertakings designed to protect the investing public.
- The term of a deferred prosecution agreement should not exceed five years. In determining the appropriate term, the staff should consider whether there is sufficient time to ensure that the undertakings in the agreement are fully implemented and the related prohibitions have adequately reduced the likelihood of future securities law violations.

Further information:

- For assistance in drafting deferred prosecution agreements, please consult with the staff in the Office of the Chief Counsel or the Chief Litigation Counsel.

6.2.4. Non-Prosecution Agreements

Basics:

A non-prosecution agreement is a written agreement between the Commission and a potential cooperating individual or company, entered in limited and appropriate circumstances, that provides that the Commission will not pursue an enforcement action against the individual or company if the individual or company agrees to, among other things: 1) cooperate truthfully and fully in the Commission's investigation and related enforcement actions; and 2) comply, under certain circumstances, with express undertakings. If the agreement is violated, the staff retains its ability to recommend an

enforcement action to the Commission against the individual or company without limitation.

Procedures:

- Prior to seeking authority to enter into a non-prosecution agreement, the staff should receive proffers from the cooperating individual and/or company.
- Non-prosecution agreements must be approved by the Commission.

Considerations:

- In virtually all cases, for individuals who have previously violated the federal securities laws, non-prosecution agreements will not be appropriate and other cooperation tools should be considered.
- Non-prosecution agreements should not be entered into in the early stages of an investigation when the role of the cooperating individuals or companies and the importance of their cooperation are unclear.
- In addition to the standard cooperation analysis set forth in Section 6.1 of the Manual, when attempting to determine whether to recommend that the Commission enter into a non-prosecution agreement, the staff should consider:
 - whether the individual or company has entered into or is likely to enter into a plea agreement with criminal prosecutors that will require them to cooperate in the Commission's investigation and related enforcement actions; and
 - whether other means of obtaining the desired cooperation are available and likely to be timely and effective.
- A non-prosecution agreement should generally include the following terms:
 - the cooperating individual or company agrees to cooperate truthfully and fully, as directed by the Division's staff, in investigations and related enforcement proceedings including, but not limited to, producing all potentially relevant non-privileged documents and materials to the Commission, responding to all inquiries, appearing for interviews, and testifying at trials and other judicial proceedings as requested by the staff, and waiving the territorial limits on service contained in Rule 45 of the Federal Rules of Civil Procedure;
 - the cooperating individual or company shall make any agreed-upon disgorgement or penalty payments;

- additional undertakings designed to protect the investing public; and
- if the individual or company violates the agreement, the Division may recommend and the Commission may pursue an enforcement action against the individual or company without limitation and not subject to the applicable statute of limitations; and
- the cooperating individual or company agrees that the Commission may use statements, information, and materials provided pursuant to the agreement against him/her/it if the individual or company violates the terms of the agreement.

Related Tool:

- Termination Notices—When an investigation has been completed as to a potential cooperating individual or company and the Division has determined, for any reason, not to recommend to the Commission an enforcement action against the individual or company, supervisors at or above the level of Assistant Director may, and in some cases are required, to send a letter informing the individual or company of the determination. If the potential cooperating individual or company is likely to provide substantial assistance and the Division has not entered into a cooperation agreement with the individual or company, these notices may be provided before the Commission's investigation is closed or before a determination has been made as to every other potential defendant or respondent in the case.

Further information:

- For assistance in drafting non-prosecution agreements, please consult with staff in the Office of the Chief Counsel or the Chief Litigation Counsel.
- For additional information about termination notices, please consult Section 2.6.2 of the Manual.

6.2.5. Immunity Requests

Introduction:

In certain circumstances, individuals may not be willing to provide testimony or cooperate without receiving protection against criminal prosecution. In appropriate circumstances, to obtain testimony and/or facilitate cooperation that will substantially assist in the enforcement of the federal securities laws, the staff may seek immunity orders or letters in order to obtain testimony and/or witness cooperation.

Basics:

When witnesses assert their Fifth Amendment privilege against self-incrimination in enforcement proceedings, the Commission may seek one of two types of immunity: statutory immunity or letter immunity. Statutory immunity permits the Commission, pursuant to 18 U.S.C. Sections 6001-6004, to seek a court order compelling the individual to give testimony or provide other information that may be necessary to the public interest, if the request is approved by the U.S. Attorney General. In contrast, letter immunity is immunity conferred by agreement between the individual and a U.S. Attorney's Office. Both types of immunity prevent the use of statements or other information provided by the individual, directly or indirectly, against the individual in any criminal case, except for perjury, giving a false statement, or obstruction of justice. Neither an immunity order nor an immunity letter, however, prevents the Commission from using the testimony or other information provided by the individual in its enforcement actions, including actions against the individual for whom the immunity order or letter was issued.

Procedures:

- Prior to seeking approval to request an immunity order or letter from the Department of Justice, the staff should preferably receive a proffer of the individual's expected testimony or have significant and reliable evidence regarding his or her ability to provide substantial assistance to the Commission's investigation or related enforcement actions.
- The Commission has delegated authority to the Director and authority has been sub-delegated to senior officers to make immunity requests to the Department of Justice. 17 C.F.R. Section 200.30-4(a).
- Prior to requesting authorization to seek an immunity order or letter from the Director of Enforcement or a designated senior officer, unless exigent circumstances exist, the staff should complete the Department of Justice witness immunity request form found at http://www.usdoj.gov/usao/eousa/foia_reading_room/usam/title9/crm00721.pdf. This form will be used for three purposes.
 - First, the form will help the staff document its basis for seeking an immunity order or letter.
 - Second, the completed form will assist senior leadership in the Division and the U.S. Department of Justice in evaluating the appropriateness of seeking an immunity order or letter.
 - Finally, if an immunity order is appropriate, the completed form will be submitted by the relevant federal prosecutor's office to the Witness Immunity Unit of the Office of Enforcement Operations at the Department

of Justice for approval—expediting the processing of the Commission's witness immunity requests.

- Upon receiving a letter of authority to seek an order to compel the testimony of a witness from the Department of Justice, a motion and proposed immunity order may be filed with the court *ex parte*. Alternatively, after receiving Department of Justice, the Commission may issue an order requiring the individual to give testimony or provide other information which he has refused to give or provide on the basis of his privilege against self incrimination. 18 U.S.C. Section 6004.
- Unless the court and/or Commission directs otherwise, immunity orders and letters will be treated as public documents.
- A copy of the draft Department of Justice witness immunity request form submitted to the Director of Enforcement or a designated senior officer and a copy of the immunity order or letter should be maintained by the senior officer submitting the request to the Department of Justice.

Considerations:

- As a general rule, immunity orders or letters should not be requested in the early stages of an investigation when the role of the cooperating individuals and the benefits of their cooperation may be unclear.
- Pursuant to 18 U.S.C. Sections 6001-6004, an immunity order should be sought only if:
 - the testimony or other information from the witness may be necessary to the public interest; and
 - the witness has refused, or is likely to refuse, to testify or provide other information on the basis of his or her privilege against self-incrimination.
- When attempting to determine whether to recommend that an immunity order or letter be sought, the staff should conduct the standard analysis set forth in Section 6.1 of the Manual.
- Since the Supreme Court has interpreted the Fifth Amendment privilege against self-incrimination to include the act of producing business records by a sole proprietorship, the Commission may request immunity for the limited purpose of obtaining such documents. *United States v. Doe*, 465 U.S. 605 (1984). However, the witness immunity request form submitted to the Department of Justice should expressly state the purpose of the application.

Further information:

For additional information regarding cooperation with the criminal authorities, please consult Sections 5.2.1 and 5.2.2 of the Manual.

6.3. Publicizing the Benefits of CooperationBasics:

The staff should provide sufficient information to the public about the nature of the Commission's cooperation program and its significant benefits.

Procedures:

As discussed in Section 6.2.2 of the Manual, where cooperation credit is being recommended to or has been authorized by the Commission in settlements, the staff should include standard language relating to cooperation in Offers, Consents, or other dispositions and reference the individual or company's cooperation in the supporting paragraphs of the related litigation and/or press releases, unless such disclosure would not advance the goals of the Commission's cooperation program or would adversely affect related ongoing investigations or proceedings.

Considerations:

- In most cases, the Commission's enforcement program is enhanced by publicizing the benefits associated with cooperating in a Commission investigation or related enforcement actions. Nevertheless, the staff retains discretion regarding whether and how to disclose the fact, manner, and extent of an individual or company's cooperation in documents filed or issued by the Commission in connection with an enforcement action.
- Since information obtained or generated during Commission investigations is generally confidential, the staff should ensure that its public statements and releases do not inadvertently disclose non-public information.
- In disclosing information regarding the benefits of cooperation in specific cases, the staff should take care to protect the identity of cooperating individuals and companies unless:
 - the identity of the individual or company has already been or will be disclosed in a public document such as an Offer, Consent, or Deferred Prosecution Agreement; or
 - the cooperating individual or company has consented to the disclosure of his/her/its identity by the Commission.

Appendix I



Amendments to the Sentencing Guidelines

May 3, 2010

This compilation contains unofficial text of amendments to the sentencing guidelines, policy statements, and commentary, and is provided only for the convenience of the user. Official text of the amendments can be found on the Commission's website at www.ussc.gov and will appear in a forthcoming edition of the Federal Register.

7. ORGANIZATIONAL GUIDELINES

Reason for Amendment: *This amendment makes several changes to Chapter Eight of the Guidelines Manual regarding the sentencing of organizations.*

First, the amendment amends the Commentary to §8B2.1 (Effective Compliance and Ethics Program) by adding an application note that clarifies the remediation efforts required to satisfy the seventh minimal requirement for an effective compliance and ethics program under subsection (b)(7). Subsection (b)(7) requires an organization, after criminal conduct has been detected, to take reasonable steps (1) to respond appropriately to the criminal conduct and (2) to prevent further similar criminal conduct.

The new application note describes the two aspects of subsection (b)(7). With respect to the first aspect, the application note provides that the organization should take reasonable steps, as warranted under the circumstances, to remedy the harm resulting from the criminal conduct. The application note further provides that such steps may include, where appropriate, providing restitution to identifiable victims, other forms of remediation, and self-reporting and cooperation with authorities. With respect to the second aspect, the application note provides that an organization should assess the compliance and ethics program and make modifications necessary to ensure the program is effective. The application note further provides that such steps should be consistent with §8B2.1(b)(5) and (c), which also require assessment and modification of the program, and may include the use of an outside professional advisor to ensure adequate assessment and implementation of any modifications.

This application note was added in response to public comment and testimony suggesting that further guidance regarding subsection (b)(7) may encourage organizations to take reasonable steps upon discovery of criminal conduct. The steps outlined by the application note are consistent with factors considered by enforcement agencies in evaluating organizational compliance and ethics practices.

Second, the amendment amends subsection (f) of §8C2.5 (Culpability Score) to create a limited exception to the general prohibition against applying the 3-level decrease for having an effective compliance and ethics program when an organization's high-level or substantial authority personnel are involved in the offense. Specifically, the amendment adds subsection (f)(3)(C), which allows an organization to receive the decrease if the organization meets four criteria: (1) the individual or individuals with operational responsibility for the compliance and ethics program have direct reporting obligations to the organization's governing authority or appropriate subgroup thereof; (2) the compliance and ethics program detected the offense before discovery outside the organization or before such discovery was reasonably likely; (3) the organization promptly reported the offense to the appropriate governmental authorities; and (4) no individual with operational responsibility for the compliance and ethics program participated in, condoned, or was willfully ignorant of the offense.

The new subsection (f)(3)(C) responds to concerns expressed in public comment and testimony that the general prohibition in §8C2.5(f)(3) operates too broadly and that internal and external reporting of criminal conduct could be better encouraged by providing an exception to that general prohibition in appropriate cases.

The amendment also adds an application note that describes the "direct reporting obligations" necessary to meet the first criterion under §8C2.5(f)(3)(C). The application note provides that an individual has "direct reporting obligations" if the individual has express authority to communicate personally to the governing

authority "promptly on any matter involving criminal conduct or potential criminal conduct" and "no less than annually on the implementation and effectiveness of the compliance and ethics program". The application note responds to public comment and testimony regarding the challenges operational compliance personnel may face when seeking to report criminal conduct to the governing authority of an organization and encourages compliance and ethics policies that provide operational compliance personnel with access to the governing authority when necessary.

Third, the amendment amends §8D1.4 (Recommended Conditions of Probation – Organizations (Policy Statement)) to augment and simplify the recommended conditions of probation for organizations. The amendment removes the distinction between conditions of probation imposed solely to enforce a monetary penalty and conditions of probation imposed for any other reason so that all conditional probation terms are available for consideration by the court in determining an appropriate sentence.

Finally, the amendment makes technical and conforming changes to various provisions in Chapter Eight.

Amendment:

§8B2.1. Effective Compliance and Ethics Program

(a) To have an effective compliance and ethics program, for purposes of subsection (f) of §8C2.5 (Culpability Score) and subsection (c)(1) of §8D1.4 (Recommended Conditions of Probation - Organizations), an organization shall—

- (1) exercise due diligence to prevent and detect criminal conduct; and
- (2) otherwise promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law.

Such compliance and ethics program shall be reasonably designed, implemented, and enforced so that the program is generally effective in preventing and detecting criminal conduct. The failure to prevent or detect the instant offense does not necessarily mean that the program is not generally effective in preventing and detecting criminal conduct.

(b) Due diligence and the promotion of an organizational culture that encourages ethical conduct and a commitment to compliance with the law within the meaning of subsection (a) minimally require the following:

- (1) The organization shall establish standards and procedures to prevent and detect criminal conduct.
- (2) (A) The organization's governing authority shall be knowledgeable about the content and operation of the compliance and ethics program and shall exercise reasonable oversight with respect to the implementation and effectiveness of the compliance and ethics program.

- (B) High-level personnel of the organization shall ensure that the organization has an effective compliance and ethics program, as described in this guideline. Specific individual(s) within high-level personnel shall be assigned overall responsibility for the compliance and ethics program.
 - (C) Specific individual(s) within the organization shall be delegated day-to-day operational responsibility for the compliance and ethics program. Individual(s) with operational responsibility shall report periodically to high-level personnel and, as appropriate, to the governing authority, or an appropriate subgroup of the governing authority, on the effectiveness of the compliance and ethics program. To carry out such operational responsibility, such individual(s) shall be given adequate resources, appropriate authority, and direct access to the governing authority or an appropriate subgroup of the governing authority.
- (3) The organization shall use reasonable efforts not to include within the substantial authority personnel of the organization any individual whom the organization knew, or should have known through the exercise of due diligence, has engaged in illegal activities or other conduct inconsistent with an effective compliance and ethics program.
- (4) (A) The organization shall take reasonable steps to communicate periodically and in a practical manner its standards and procedures, and other aspects of the compliance and ethics program, to the individuals referred to in ~~subdivision~~subparagraph (B) by conducting effective training programs and otherwise disseminating information appropriate to such individuals' respective roles and responsibilities.
- (B) The individuals referred to in ~~subdivision~~subparagraph (A) are the members of the governing authority, high-level personnel, substantial authority personnel, the organization's employees, and, as appropriate, the organization's agents.
- (5) The organization shall take reasonable steps—
- (A) to ensure that the organization's compliance and ethics program is followed, including monitoring and auditing to detect criminal conduct;
 - (B) to evaluate periodically the effectiveness of the organization's compliance and ethics program; and
 - (C) to have and publicize a system, which may include mechanisms that allow for anonymity or confidentiality, whereby the

organization's employees and agents may report or seek guidance regarding potential or actual criminal conduct without fear of retaliation.

- (6) The organization's compliance and ethics program shall be promoted and enforced consistently throughout the organization through (A) appropriate incentives to perform in accordance with the compliance and ethics program; and (B) appropriate disciplinary measures for engaging in criminal conduct and for failing to take reasonable steps to prevent or detect criminal conduct.
- (7) After criminal conduct has been detected, the organization shall take reasonable steps to respond appropriately to the criminal conduct and to prevent further similar criminal conduct, including making any necessary modifications to the organization's compliance and ethics program.
- (c) In implementing subsection (b), the organization shall periodically assess the risk of criminal conduct and shall take appropriate steps to design, implement, or modify each requirement set forth in subsection (b) to reduce the risk of criminal conduct identified through this process.

Commentary

Application Notes:

* * *

2. Factors to Consider in Meeting Requirements of this Guideline.—

* * *

(D) Recurrence of Similar Misconduct.—*Recurrence of similar misconduct creates doubt regarding whether the organization took reasonable steps to meet the requirements of this guideline. For purposes of this subdivisionsubparagraph, "similar misconduct" has the meaning given that term in the Commentary to §8A1.2 (Application Instructions - Organizations).*

* * *

6. Application of Subsection (b)(7).—*Subsection (b)(7) has two aspects.*

First, the organization should respond appropriately to the criminal conduct. The organization should take reasonable steps, as warranted under the circumstances, to remedy the harm resulting from the criminal conduct. These steps may include, where appropriate, providing restitution to identifiable victims, as well as other forms of remediation. Other reasonable steps to respond appropriately to the criminal conduct may include self-reporting and cooperation with authorities.

Second, the organization should act appropriately to prevent further similar criminal conduct, including assessing the compliance and ethics program and making modifications necessary to ensure the program is effective. The steps taken should be consistent with subsections (b)(5) and (c) and may include the use of an outside professional advisor to ensure adequate assessment and implementation of any modifications:

67. Application of Subsection (c).—To meet the requirements of subsection (c), an organization shall:

* * *

- (B) *Prioritize periodically, as appropriate, the actions taken pursuant to any requirement set forth in subsection (b), in order to focus on preventing and detecting the criminal conduct identified under ~~subdivision~~subparagraph (A) of this note as most serious, and most likely, to occur.*
- (C) *Modify, as appropriate, the actions taken pursuant to any requirement set forth in subsection (b) to reduce the risk of criminal conduct identified under ~~subdivisions~~subparagraph (A) of this note as most serious, and most likely, to occur.*

Background: *This section sets forth the requirements for an effective compliance and ethics program. This section responds to section 805(a)(2)(5) of the Sarbanes-Oxley Act of 2002, Public Law 107-204, which directed the Commission to review and amend, as appropriate, the guidelines and related policy statements to ensure that the guidelines that apply to organizations in this chapter "are sufficient to deter and punish organizational criminal misconduct."*

The requirements set forth in this guideline are intended to achieve reasonable prevention and detection of criminal conduct for which the organization would be vicariously liable. The prior diligence of an organization in seeking to prevent and detect criminal conduct has a direct bearing on the appropriate penalties and probation terms for the organization if it is convicted and sentenced for a criminal offense.

* * *

§8C2.5. Culpability Score

(a) Start with 5 points and apply subsections (b) through (g) below.

(b) Involvement in or Tolerance of Criminal Activity

If more than one applies, use the greatest:

(1) If --

(A) the organization had 5,000 or more employees and

(i) an individual within high-level personnel of the organization participated in, condoned, or was willfully ignorant of the offense; or

(ii) tolerance of the offense by substantial authority personnel was pervasive throughout the organization; or

(B) the unit of the organization within which the offense was committed had 5,000 or more employees and

(i) an individual within high-level personnel of the unit participated in, condoned, or was willfully ignorant of the offense; or

(ii) tolerance of the offense by substantial authority personnel was pervasive throughout such unit,

add 5 points; or

(2) If --

(A) the organization had 1,000 or more employees and

(i) an individual within high-level personnel of the organization participated in, condoned, or was willfully ignorant of the offense; or

(ii) tolerance of the offense by substantial authority personnel was pervasive throughout the organization; or

(B) the unit of the organization within which the offense was committed had 1,000 or more employees and

(i) an individual within high-level personnel of the unit participated in, condoned, or was willfully ignorant of the offense; or

(ii) tolerance of the offense by substantial authority personnel was pervasive throughout such unit,

add 4 points; or

(3) If --

(A) the organization had 200 or more employees and

(i) an individual within high-level personnel of the organization participated in, condoned, or was willfully ignorant of the offense; or

(ii) tolerance of the offense by substantial authority personnel

was pervasive throughout the organization; or

- (B) the unit of the organization within which the offense was committed had 200 or more employees and
- (i) an individual within high-level personnel of the unit participated in, condoned, or was willfully ignorant of the offense; or
 - (ii) tolerance of the offense by substantial authority personnel was pervasive throughout such unit,

add 3 points; or

- (4) If the organization had 50 or more employees and an individual within substantial authority personnel participated in, condoned, or was willfully ignorant of the offense, add 2 points; or
- (5) If the organization had 10 or more employees and an individual within substantial authority personnel participated in, condoned, or was willfully ignorant of the offense, add 1 point.

(c) Prior History

If more than one applies, use the greater:

- (1) If the organization (or separately managed line of business) committed any part of the instant offense less than 10 years after (A) a criminal adjudication based on similar misconduct; or (B) civil or administrative adjudication(s) based on two or more separate instances of similar misconduct, add 1 point; or
- (2) If the organization (or separately managed line of business) committed any part of the instant offense less than 5 years after (A) a criminal adjudication based on similar misconduct; or (B) civil or administrative adjudication(s) based on two or more separate instances of similar misconduct, add 2 points.

(d) Violation of an Order

If more than one applies, use the greater:

- (1) (A) If the commission of the instant offense violated a judicial order or injunction, other than a violation of a condition of probation; or (B) if the organization (or separately managed line of business) violated a condition of probation by engaging in similar misconduct, *i.e.*, misconduct similar to that for which it was placed on probation, add 2 points; or

- (2) If the commission of the instant offense violated a condition of probation, add 1 point.

(e) Obstruction of Justice

If the organization willfully obstructed or impeded, attempted to obstruct or impede, or aided, abetted, or encouraged obstruction of justice during the investigation, prosecution, or sentencing of the instant offense, or, with knowledge thereof, failed to take reasonable steps to prevent such obstruction or impedance or attempted obstruction or impedance, add 3 points.

(f) Effective Compliance and Ethics Program

- (1) If the offense occurred even though the organization had in place at the time of the offense an effective compliance and ethics program, as provided in §8B2.1 (Effective Compliance and Ethics Program), subtract 3 points.

- (2) Subsection (f)(1) shall not apply if, after becoming aware of an offense, the organization unreasonably delayed reporting the offense to appropriate governmental authorities.

- (3) (A) Except as provided in ~~subdivision (B)~~ subparagraphs (B) and (C), subsection (f)(1) shall not apply if an individual within high-level personnel of the organization, a person within high-level personnel of the unit of the organization within which the offense was committed where the unit had 200 or more employees, or an individual described in §8B2.1(b)(2)(B) or (C), participated in, condoned, or was willfully ignorant of the offense.

- (B) There is a rebuttable presumption, for purposes of subsection (f)(1), that the organization did not have an effective compliance and ethics program if an individual—

- (i) within high-level personnel of a small organization; or
 (ii) within substantial authority personnel, but not within high-level personnel, of any organization,

participated in, condoned, or was willfully ignorant of, the offense.

- (C) Subparagraphs (A) and (B) shall not apply if—

- (i) the individual or individuals with operational responsibility for the compliance and ethics program (see §8B2.1(b)(2)(C)) have direct reporting obligations to the governing authority or an appropriate subgroup thereof

(e.g., an audit committee of the board of directors);

- (ii) the compliance and ethics program detected the offense before discovery outside the organization or before such discovery was reasonably likely;
- (iii) the organization promptly reported the offense to appropriate governmental authorities; and
- (iv) no individual with operational responsibility for the compliance and ethics program participated in, condoned, or was willfully ignorant of the offense.

(g) Self-Reporting, Cooperation, and Acceptance of Responsibility

If more than one applies, use the greatest:

- (1) If the organization (A) prior to an imminent threat of disclosure or government investigation; and (B) within a reasonably prompt time after becoming aware of the offense, reported the offense to appropriate governmental authorities, fully cooperated in the investigation, and clearly demonstrated recognition and affirmative acceptance of responsibility for its criminal conduct, subtract 5 points; or
- (2) If the organization fully cooperated in the investigation and clearly demonstrated recognition and affirmative acceptance of responsibility for its criminal conduct, subtract 2 points; or
- (3) If the organization clearly demonstrated recognition and affirmative acceptance of responsibility for its criminal conduct, subtract 1 point.

Commentary

Application Notes:

* * *

- 10. *Subsection (f)(2) contemplates that the organization will be allowed a reasonable period of time to conduct an internal investigation. In addition, no reporting is required by subsection (f)(2) or (f)(3)(C)(iii) if the organization reasonably concluded, based on the information then available, that no offense had been committed.*
- 11. *For purposes of subsection (f)(3)(C)(i), an individual has "direct reporting obligations" to the governing authority or an appropriate subgroup thereof if the individual has express authority to communicate personally to the governing authority or appropriate subgroup thereof (A) promptly*

on any matter involving criminal conduct or potential criminal conduct, and (B) no less than annually on the implementation and effectiveness of the compliance and ethics program.

- †12. "Appropriate governmental authorities," as used in subsections (f) and (g)(1), means the federal or state law enforcement, regulatory, or program officials having jurisdiction over such matter. To qualify for a reduction under subsection (g)(1), the report to appropriate governmental authorities must be made under the direction of the organization.
- †13. To qualify for a reduction under subsection (g)(1) or (g)(2), cooperation must be both timely and thorough. To be timely, the cooperation must begin essentially at the same time as the organization is officially notified of a criminal investigation. To be thorough, the cooperation should include the disclosure of all pertinent information known by the organization. A prime test of whether the organization has disclosed all pertinent information is whether the information is sufficient for law enforcement personnel to identify the nature and extent of the offense and the individual(s) responsible for the criminal conduct. However, the cooperation to be measured is the cooperation of the organization itself, not the cooperation of individuals within the organization. If, because of the lack of cooperation of particular individual(s), neither the organization nor law enforcement personnel are able to identify the culpable individual(s) within the organization despite the organization's efforts to cooperate fully, the organization may still be given credit for full cooperation.
- †14. Entry of a plea of guilty prior to the commencement of trial combined with truthful admission of involvement in the offense and related conduct ordinarily will constitute significant evidence of affirmative acceptance of responsibility under subsection (g), unless outweighed by conduct of the organization that is inconsistent with such acceptance of responsibility. This adjustment is not intended to apply to an organization that puts the government to its burden of proof at trial by denying the essential factual elements of guilt, is convicted, and only then admits guilt and expresses remorse. Conviction by trial, however, does not automatically preclude an organization from consideration for such a reduction. In rare situations, an organization may clearly demonstrate an acceptance of responsibility for its criminal conduct even though it exercises its constitutional right to a trial. This may occur, for example, where an organization goes to trial to assert and preserve issues that do not relate to factual guilt (e.g., to make a constitutional challenge to a statute or a challenge to the applicability of a statute to its conduct). In each such instance, however, a determination that an organization has accepted responsibility will be based primarily upon pretrial statements and conduct.
- †15. In making a determination with respect to subsection (g), the court may determine that the chief executive officer or highest ranking employee of an organization should appear at sentencing in order to signify that the organization has clearly demonstrated recognition and affirmative acceptance of responsibility.

Background: The increased culpability scores under subsection (b) are based on three interrelated principles. First, an organization is more culpable when individuals who manage the organization or who have substantial discretion in acting for the organization participate in, condone, or are willfully ignorant of criminal conduct. Second, as organizations become larger and their managements become more professional, participation in, condonation of, or willful ignorance of criminal conduct by such management is increasingly a breach of trust or abuse of position. Third, as organizations increase in size, the risk of

criminal conduct beyond that reflected in the instant offense also increases whenever management's tolerance of that offense is pervasive. Because of the continuum of sizes of organizations and professionalization of management, subsection (b) gradually increases the culpability score based upon the size of the organization and the level and extent of the substantial authority personnel involvement.

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§8D1.4. Recommended Conditions of Probation - Organizations (Policy Statement)

- (a) The court may order the organization, at its expense and in the format and media specified by the court, to publicize the nature of the offense committed, the fact of conviction, the nature of the punishment imposed, and the steps that will be taken to prevent the recurrence of similar offenses.
- (b) If probation is imposed under §8D1.1(a)(2), the following conditions may be appropriate ~~to the extent they appear necessary to safeguard the organization's ability to pay any deferred portion of an order of restitution, fine, or assessment:~~
 - (1) The organization shall develop and submit to the court an effective compliance and ethics program consistent with §8B2.1 (Effective Compliance and Ethics Program). The organization shall include in its submission a schedule for implementation of the compliance and ethics program.
 - (2) Upon approval by the court of a program referred to in paragraph (1), the organization shall notify its employees and shareholders of its criminal behavior and its program referred to in paragraph (1). Such notice shall be in a form prescribed by the court.
 - (±3) The organization shall make periodic submissions to the court or probation officer, at intervals specified by the court, (A) reporting on the organization's financial condition and results of business operations, and accounting for the disposition of all funds received, and (B) reporting on the organization's progress in implementing the program referred to in paragraph (1). Among other things, reports under subparagraph (B) shall disclose any criminal prosecution, civil litigation, or administrative proceeding commenced against the organization, or any investigation or formal inquiry by governmental authorities of which the organization learned since its last report.
 - (4) The organization shall notify the court or probation officer immediately upon learning of (A) any material adverse change in its business or financial condition or prospects, or (B) the commencement of any bankruptcy proceeding, major civil litigation, criminal prosecution, or administrative proceeding against the organization, or any investigation or formal inquiry by governmental authorities regarding the organization.



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