



ACC'S CLO THINKTANK SERIES 2005

"CORPORATE LIABILITY: PROSECUTORIAL TRENDS AND TACTICS"

Hosted by Bill Lytton, CLO of Tyco International Ltd.

**September 30, The Ritz Carlton New York- Central Park
10:00 a.m. – 2:00 p.m.**

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Participants' Briefing Materials

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Summary/ Outline of Discussion Topics

The following outline is intended to provide a short overview of some of the issues at the heart of this discussion topic. There may be other issues we've not identified or perspectives on the identified issues that are not adequately represented in the outline: you should feel free to raise these additional thoughts, as you like. The outline is merely intended as a starting point to help you identify discussion topics and tee up your conversation.

Corporate Liability- Prosecutorial Trends and Tactics

A. Corporate Liability

1. Justice Department factors for criminally charging organizations- *The Thompson Memo.*

Factors include in summary form:

- Nature and seriousness of the offense
- Pervasiveness of wrongdoing (including complicity/condonation of wrongdoing by management)
- History of similar corporate conduct
- Cooperation and self-disclosure—including, if necessary, waiver of attorney-client privilege and work product protection
- Compliance program- existence and adequacy of
- Remedial actions
- Collateral consequences (including disproportionate harm to shareholders, pension holders, and employees not proven personally culpable and impact on public)
- Adequacy of prosecution of individuals
- Adequacy of remedies such as civil or regulatory enforcement actions

2. State Attorney General Actions

- Targeting industries
- Concept of “no stone unturned” in protecting the public
- Motivating factors and personalities vary - impacts and implications

3. SEC Enforcement

- In-house lawyers as “gatekeepers”- Cutler speech
- Different approach for in-house lawyers vs. outside counsel: enforcement against in-house counsel without independent finding of misconduct; no enforcement against outside counsel unless outside lawyer held civil or criminally liable or disciplined by the bar

- Some Notable Elements in SEC enforcement cases against in-house counsel:
 - > CLOs are nearly always the target
 - > Inside lawyers who rely on outside counsel are seldom targets
 - > Personal financial rewards are not necessary to prompt enforcement
 - > Underlying conduct: many cases involve disclosures/ omissions in disclosures
 - > Apparent imposition of a duty for generalist lawyers to seek expert legal and technical advice (generalist’s reliance on inside technical expert or seeing ‘red flag’ and failing to seek outside advice “is not well-received”)
 - > Corporate failure, holding several corporate offices, and/or failing to raise troublesome issues with the Board appear to be factors that can raise the risk for enforcement

4. U.S. Sentencing Guidelines for Organizations

- Amended as of November 1, 2004; Guideline status- permissive references rather than mandatory guidelines per 2004-5 case law in *Blakely*, *Booker* and *Fanfan* cases.
- Emerging activity on capitol hill suggests strong interest in proposing new mandatory guidelines; strategic starting point is likely to be the current guidelines
- Define minimum criteria for an Effective Compliance and Ethics Program (ECEP)- relevant both as mitigating sentencing factor and as charging factor; amended guidelines take an “all-or-nothing” approach to having an ECEP
- Credits not available to companies that don’t cooperate; cooperation linked to possible waiver of attorney-client privilege and attorney work product doctrines (New Commentary Application Note 12 to 8C2.5 :“Waiver of attorney-client privilege and of work product protections is not a prerequisite to reduction of the culpability score... unless such waiver is necessary in order to provide timely and thorough disclosure of all pertinent information known to the organization)
- Provision disallowing reduction in culpability score if organization doesn’t make a timely report of the offense to governmental authorities—even if the organization has an ECEP
- Provision disallowing culpability score reduction if high-level personnel participated in, condoned or were willfully ignorant of the violation
- Challenges/Opportunities for Change: are there provisions in the amended guidelines that present challenges and require modification or clarification?

5. Compliance and Ethics Program- factor in corporate charging decisions and as a mitigating factor for organizational sentencing

- New and expanded provisions defining an ECEP included in the Sentencing Guidelines- the program must also promote an organizational culture that encourages ethical conduct and a commitment to compliance with law
- Demonstrating existence of an ECEP; policies and structure
- Organizational structure for compliance and reporting relationship to the law department and/or the Board; handled within the law department vs. stand-alone business model?
- Implications of CLO as Chief Compliance Officer and compliance committee participant; changes to role or structure in light of recent prosecutorial trends? Practical strategies for tracking roles and advice?
- Mechanisms and role of Board in implementing program oversight; circumstances and approaches for consulting with outside counsel

6. Cooperation- factor in both corporate charging decisions and as a mitigating factor for sentencing

- Charging factor in Thompson memo: “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.”
- Credit factor in U.S. Sentencing Guidelines: cooperation of the organization must be timely (e.g., begin essentially at the same time officially notified of a criminal investigation) and thorough
- Process/policy for cooperation: who within the company decides the overall approach to cooperation and how is this communicated to the organization? How is cooperation communicated to the government?
- Governmental Inquiries/Investigations: Experiences? How is government communicating its assessment of cooperation? Is waiver of privilege being demanded? Variations among agencies, state and federal AGs, etc.?

7. Internal Investigations- impacts on process and role of in-house lawyers

- With cooperation as both a charging factor and a “credit” factor for sentencing, what are the implications for conducting internal investigations? Are investigations conducted with an understanding that the results and/or a written report will likely be provided to the government? Are reports provided or underlying facts discussed?
- How does this impact the scope and approach for conducting the investigation?

- What factors are considered in determining whether to prepare a written report?
- Is privilege an issue? What is the role of lawyers (in-house) on the investigative team?
- Are there two internal investigations (one that might be provided to the government and a second for which privilege may be claimed)?
- Guidance or training on performing the investigation and writing the report?
- How are corporate miranda warnings provided to employee interviewees (verbally, in writing, signed statement, etc.)?

8. Privilege in the Prosecutorial Context

- Federal agency enforcement actions identify lawyers as “gatekeepers” and require waiver as evidence of cooperation
- Privilege waiver cases are not making it to courts; waiver demands happen outside of the courtroom; the judiciary can’t protect the evidentiary privilege
- The entity owns the privilege- what is the process within the organization for granting waiver? Short vs. long-term interests
- Is the analysis different depending on the stage (e.g., as a consideration for charging factors vs. sentencing)?
- Limited, subject matter or selected waiver options: trying to hold the line against more costly/subsequent third party suits
- Does the potential for waiver impact the decision to involve outside counsel?
- Is there a chilling effect on preventive law counseling and ability to perform effective internal investigations?
- Has your company successfully implemented strategies to demonstrate cooperation while also preserving privilege?
- Do clients care or even understand privilege? Does the presence or absence of privilege affect the way they behave? Is it a priority for client relationships? Does it really matter to anyone except the lawyers?

Links to Resources:

(http://www.usdoj.gov/dag/speech/2006/mcnulty_memo.pdf)

(<http://www.sec.gov/news/speech/spch092004smc.htm>)

(<http://www.acca.com/protected/article/ethics/seccrimproceed.pdf>)

(http://www.ussc.gov/2004guid/8b2_1.htm)

(<http://acc.com/resource/v5708>)

(<http://acc.com/resource/v5715>)

(<http://acc.com/resource/v6033>)

B. Individual Liability-- The Reality: Corporate Counsel in the Cross-hairs

1. ABA Model Rule 1.13 and Sarbox 307 Attorney Professional Conduct Standards: “reporting-up” requirements and exposure to sanctions or disciplinary action

- Up-the-ladder reporting systems and channels for reporting (supervisory attorneys, audit committees, CLO, QLCC, etc.)
- Scope of reportable matters: broader than Sarbox 307?
- Are certifications of individual lawyers required?
- What type of ethics/compliance reporting training is provided to in-house lawyers? How do supervisory lawyers or CLOs distinguish when discussions are 307 discussions versus requests for guidance?
- Implications and methods for communicating Sarbox 307 policy and program requirements to clients
- Role of in-house lawyer: Do the standards have a chilling effect on client willingness to seek preventive legal guidance?
- Interface with outside counsel: Do they sign onto your policy? Do you receive copies of their policies? Are there requirements for them to notify designated individuals within the law department simultaneously with performing their own internal review of whether a Sarbox 307 issue has been identified?
- Are in-house lawyers asking about corporate protections available to them in light of their increasing exposure (vis-à-vis the SEC and the bar) pursuant to Sarbox 307?

2. In-House Lawyer Liability and Lawyers as Witnesses—contexts and consequences

- Interviews of in-house lawyers by outside counsel engaged by the Board or a Board Committee
- Interviews of in-house lawyers by public regulators and law enforcement; access to in-house lawyers as part of the organization’s cooperation
- Interviews of in-house lawyers in jurisdictions where privilege is not recognized
- Civil litigation depositions and other forms of discovery: case law trends allow depositions of opposing non-litigation counsel if the deposition will not elicit privileged information regarding litigation strategy in the pending case (Shelton, Pamida, Philip Morris)
- Grand Jury or Trial Subpoenas issued to in-house lawyers: issues relating to privileged information
- Client assertions of advice-of-counsel defense
- Testimony of in-house lawyers as part of federal sentencing “credit”

- Consequences of having in-house lawyers provide testimony can be significant, including waiver of attorney-client privilege and attorney work product doctrines, disqualification of lawyer as in-house counsel on the matter, and more
- Benefits of having in-house lawyers provide testimony can be significant, including opportunity to receive more favorable treatment for organization in charging decisions, receipt of cooperation “credit” in organizational sentencing, quicker resolution

3. Practical Considerations of In-House Lawyer as Witness

- Strategies for taking care not to blur legal and business functions for in-house lawyers: is this a realistic exercise for a lawyer in the cross-hairs?
- Training for in-house lawyers and clients on proper use of and protections offered by attorney-client privilege and attorney work product doctrine
- Implications of non-waiver and limited waiver agreements; exposure to third party claims and suits
- Responsibility for determining whether the in-house lawyer may testify- who decides? Should company representatives obtain independent legal advice on risks and benefits of testimony by in-house counsel?
- Implications of having an in-house lawyer execute affidavits and impacts on potential for becoming a fact witness
- Staffing of team for conducting internal investigations- consider including more than one lawyer, and/or a business person or outside counsel
- Issues surrounding retaining and paying for outside counsel to represent in-house lawyers performing roles as witnesses

4. Impact on CLOs- criminal cases

- Focus of criminal cases is almost entirely against CLOs
- About a dozen cases
- USDOJ Corporate Fraud Task Force
- Nearly all prosecutions were against in-house lawyers who also were subject to SEC administrative sanctions
- Some common threads noted in materials: big losses increase risk of prosecution; perjury and obstruction of justice as crimes charged; mere knowledge of transaction later deemed to be financial fraud does not appear to be sufficient to charge; almost absence of actions when inside lawyers have relied upon outside legal advice; no prosecutions where alleged fraud is complex and propriety debatable

Links to Resources:

(<http://www.acca.com/resource/v6328>)

(<http://acc.com/resource/v6367>)

C. Indemnification & Insurance Issues

1. Directors & Officers Liability Insurance Coverage

- Scope of coverage: which in-house lawyers are covered? Does the insurance cover claims against attorney-officers for legal advice or is that advice considered to be professional services for which coverage is excluded?
- Trends in negotiating coverage: what types of information are underwriters seeking in discussions to cover in-house lawyers? What types of exclusions? How are premiums being impacted?
- Challenges in trimming exclusions: what are your experiences in negotiating and trying to carve back exclusions relating to in-house lawyers?
- Success stories/practical considerations in negotiating coverage?

2. Employed Lawyers Professional Liability Policies

- What are the benefits and limitations of having this form of coverage?
- Experiences negotiating these policies? Trends in negotiating coverage?
- Are in-house lawyers asking for this coverage?

3. Indemnification

- Within corporate by-laws
- Mandatory statutory indemnifications in some states
- Indemnification Policies that apply broadly
- Individual Indemnification Agreements
- ACC amicus brief in US v. Lake and Wittig: asserting need for and public interest in preserving right to advancement of legal fees and expenses under pre-existing, generally applicable, statutorily authorized corporate policies
- Scope of coverage and issues relating to advancement of costs- view that full cooperation with the government requires refusal to pay legal costs for individuals who are unwilling to speak with prosecutors
- Prosecutorial trends, Sarbox 307 responsibilities and trends in requests for indemnification of in-house lawyers

Links to Resources:

(<http://www.acca.com/resource/v6300>)