Zuckerman Spaeder

Outside Counsel

ENFORCEMENT AND COMPLIANCE STRATEGIES

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IN THIS ISSUE

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Internal Investigations: You May Be Working for the Government

*by Lisa A. Cahill**

When you undertake an internal corporate investigation, whether as in-house counsel or as outside counsel, you may, as a practical matter, have been deputized by the U.S. Department of Justice ("DOJ").

U.S. Attorneys' Offices are increasingly requiring corporations to waive the attorney-client and work product privileges and to disclose, at a minimum, the factual findings of any internal investigation—on pain of corporate prosecution or of harsher charges and penalties against the company. Indeed, a company's decision to waive the attorney-client and work product privileges and to turn over its internal investigation is recognized in DOJ Guidelines as one of eight factors guiding the decision to prosecute a corporation. June 16, 1999, Memorandum from Deputy Attorney General Eric Holder titled "Bringing Criminal Charges Against Corporations" ("June 1999 DOJ Memorandum"). (Available on ACCA Online℠). (www.acca.com/gcadvocate/advocacy/holder.html).

ACCA has criticized the government's demand for privileged materials from internal investigations, complaining in a May 12, 2000 letter to the Department of Justice that its guidelines are "bad public policy." (see www.acca.com/gcadvocate/advocacy/holder.html) However true that thought may be, DOJ has continued its demands for privileged materials from internal investigations.

The problems such demands pose are enormous:

- Production to the government of materials from an internal investigation may waive all objections to producing the same materials to civil litigants. This waiver is the practical equivalent of handing over a loaded gun to the plaintiffs' bar.

- If a client agrees, at your recommendation, to waive privileges and to produce its internal report, but the cooperation deal thereafter goes south, you may have effectively drafted the indictment against your own client. Don't be surprised if that indictment alleges facts discovered in the internal investigation, facts the government might have otherwise been unable to discover.

- The possibility of waiver and production can compromise the reliability of the internal investigation. Not surprisingly, employees who get wind that the corporation may be handing over interview notes to prosecutors may become unavailable for interviews or go scurrying to find their own counsel.

These problems notwithstanding, the issue generally is not whether to conduct an internal investigation or whether to disclose it to prosecutors. Recall that, in 1995, Daiwa senior management learned of sub-

stantial unauthorized trades, but delayed for several weeks notifying U.S. regulators. As a consequence, the Federal Reserve shut down Daiwa's U.S. banking operations, and the bank was indicted on 24 conspiracy and fraud counts in the Southern District of New York. It pleaded guilty to some of those charges in February 1996, and ultimately paid a $340 million fine. And no lawyer worth his or her salt, having committed a client to a course of cooperation and cognizant of potentially substantial penalties under the U.S. Sentencing Guidelines, is going to defy a government demand for waiver of privileges, thereby potentially jeopardizing the client's 5K letter, which the government can write in order to permit a lighter sentence.

So, as a practical matter, if it is impossible to avoid an internal investigation and if the company may have to turn the results of such an investigation over to the government, how should you proceed? Carefully, taking into account at least the following considerations:

- Use care in taking notes and in summarizing interviews in memos. Don't be casual or sloppy because the notes and memos are not just for your own use. They will be picked apart for meaning by adversaries, civil and criminal, who may argue that they mean something very different from what you had had in mind.

- If adversaries are going to use your notes and memos and perhaps your testimony, about an investigation, you may want to be sure that your documents lock in certain information from witnesses. For example, witnesses who are favorable could change their story later under pressure, and unfavorable witnesses may later embellish what they have to say. You may also want to record impeaching material. Further, if damaging witnesses change their stories during one or more interviews or seem evasive or to be lying, you may want to record that situation vividly.

- Fairness (and ABA Model Rules 1.13(d) and 4.3) may compel you to tell employees and officers, before you interview them, that you do not represent them and that you are conducting an investigation for the company that may be turned over to prosecutors. Although witnesses may become reticent or hire their own counsel and clam up, you will not be misleading anyone.

- Any report concerning the internal investigation should carefully distinguish recitations of documents found and statements made by witnesses from counsel's own opinions, analysis, and advice concerning the potential or existing criminal investigation. The possibility remains that the government will not insist on the revelation of counsel's own mental impressions and of the advice it has given to the client concerning the government, its adversary, although there is no guarantee. DOJ's 1999 Memorandum provides that 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."

Ultimately, internal investigations usually are not just for internal use anymore. This shift makes them more important than ever. Corporate counsel need them to understand the facts themselves and to defend the company and address any underlying problems. But in serving those traditional ends the record you are creating will affect potential civil and criminal litigation, and you need to keep that fact in mind as you are creating the record. ■

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Elements of an Effective Antitrust Compliance Program

*by Ronald B. Ravikoff and Michael S. Pasano**

Companies increasingly recognize the value of adopting sophisticated compliance programs to ensure that their employees remain within the bounds of federal and state laws that prohibit price fixing and related activities.

A compliance program is worthwhile for the same reason an insurance policy is: to cover potentially devastating risks. Violations of criminal antitrust laws may result in felony convictions punishable by imprisonment and fines as high as $350,000 for individuals and $10,000,000 for corporations. Short of criminal liability, violations of antitrust laws may give rise to government investigations under both the Federal Trade Commission Act and similar state acts. Enforcement activity typically leads to private litigation, with the threat of treble damages, disruptive injunctions, and huge attorneys' fees.

In addition to preventing antitrust violations, the existence of an antitrust compliance program may serve to mitigate the consequences of a violation that occurs in spite of the policy. The federal sentencing guidelines explicitly provide for lower penalties if a corporation has an effective program to prevent and detect violations of law (§ 8C2.5(f)). And some courts now instruct the jury that the existence of an antitrust compliance program may be evidence that the corporation itself did not intend to violate the antitrust laws.

An antitrust compliance program also educates company employees about permissible conduct under the antitrust laws. Without such training, the company could be at a competitive disadvantage because employees might refrain from aggressive business practices they mistakenly believe are illegal.

Most antitrust compliance programs consist of three elements: (1) audit of existing practices, (2) preparation and maintenance of an antitrust policy guidebook, and (3) ongoing employee education.

The Antitrust Audit

The first step in the establishment of an antitrust compliance program is ensuring that the company currently complies with all antitrust laws. Typically, companies retain outside counsel to review existing policies and practices. Such an audit identifies problem areas requiring immediate corrective action and pinpoints aspects of the business to which the antitrust laws have particular relevance.

An antitrust audit normally consists of interviews with employees and a review of company documents. Counsel conducts interviews in small groups within the company, such as senior managers, those responsible for pricing decisions, anyone active in industry trade associations, and other key decision-makers.

Such interviews explore the company's contacts with competitors in the course of everyday business operations, trade association meetings, and social gatherings. Audit interviews address such subjects as parallel behavior, common customers, common sources of products, price verification activities, patent arrangements involving competitors, joint ventures, and director interlocks. Trade association activities are especially sensitive.

It is important to examine the process by which the company makes pricing policy decisions and, in particular, how the company generates price variations, such as discounts. For example, counsel may note that a company's quantity or volume discounts favor only a few large buyers when, under antitrust laws, the company should generally be making its services and facilities available to competing customers on a proportionately equal basis. Also, random checks of invoices and other documents concerning the delivery of goods for no charge may reveal hidden problems. Counsel must determine whether the company sells two or more separate products or services together and how the company prices those items.

It is also useful to examine the company's relationship with its distributors because distributor termination policies and restrictions on distributor territories may generate antitrust litigation. For example, dual distribution, in which the company sells directly to customers, as well as selling to its own distributors, may give rise to antitrust concerns. A related

question is whether a particularly powerful buyer uses its leverage to extract special terms or discriminatory discounts to stifle competition. Similarly, reciprocal buying agreements may implicate the antitrust laws.

The document review associated with an antitrust audit normally involves a sampling of company documents. The first step in a document review is to ascertain whether the company has an adequate document control program. If no such program exists, counsel would help the company implement one.

It is not uncommon for a document review to uncover troublesome material. How should a company handle such documents? If the document is related to an area that involves an investigation or pending litigation, the company must preserve it. In the absence of investigation or litigation, the company may properly destroy such documents pursuant to an existing document control (retention/destruction) policy. It may be appropriate for a company executive to write a memorandum to the file to accompany the document, disclaiming corporate acquiescence, with a copy of that memo going to the document's author instructing him or her to desist from such conduct in the future.

The Antitrust Guidebook

The next step in the compliance program is the publication of a written policy statement or guidebook. The format of the policy statement may range from a simple letter to a full-fledged booklet, depending on the nature of the company.

The central purpose of the exercise is to provide clear guidance to company employees so that potential antitrust problems may be avoided. At a minimum, all company personnel who are likely to have any contact with customers, competitors, or suppliers should receive a copy. It may be useful to emphasize the importance of the policy by requiring each recipient to complete a form acknowledging receipt and attesting that he or she has read the policy.

At the outset, the guidebook should establish a goal of full compliance with the antitrust laws and should repeatedly encourage employees to seek guidance when antitrust questions arise. The guidebook must explain with specificity the harsh sanctions available under the antitrust laws and should also describe the employment-related consequences for employees who violate the company's antitrust compliance policy.

The guidebook should contain a nontechnical discussion of antitrust laws and the philosophy behind them. It may be useful to illustrate potential antitrust violations, perhaps supplemented with a set of basic "do's and don't's." It is particularly important to explain the concept of "contract, combination or conspiracy" so that employees understand the breadth of activity encompassed by antitrust laws.

An important element of the guidebook is a recitation of the company's document generation and retention policies. A well-run company should encourage the generation of documents that record in some detail price changes and contacts with competitors in order to have helpful evidence should the need arise.

The guidebook should, of course, be drafted with the recognition that it may eventually be read by those outside the company, including government agents or litigation adversaries.

Ongoing Employee Education

Once a company has developed and disseminated its antitrust policy, it must reinforce the policy through regular education of company personnel. For example, the antitrust policy may need to be updated to reflect new legal developments, and the materials distributed to employees should be updated as the company's business evolves.

In addition, the company should schedule antitrust compliance meetings on a regular basis and no less than once a year. These meetings should occur on a department-by-department basis in order to emphasize antitrust issues of concern to different sectors of the company. Such meetings should allow for discussion generated by employee questions. A question-and-answer format permits counsel to ascertain potential problems and to suggest areas where additional compliance education would be appropriate. ■

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Think Twice About Contacts with Another Lawyer's Client

*by William W. Taylor III and Norman L. Eisen**

Lawyers often do not think about the rule against contacts with represented persons. Yet mistakes can be serious.

Allegations about such contacts result in disciplinary proceedings. Courts can order the production of all notes and memoranda by a lawyer concerning a particular contact. Evidence obtained as a result of the contact may be kept out at trial. Counsel may be disqualified.

The lawyer who is aware of the details of the rule governing contacts with represented persons will not miss the opportunity to use the rule against the other side—and to avoid falling victim to the rule.

Typical Problems Facing Corporate Counsel

- Your company has a dispute with another company. A senior official of the other company, who is a friend of yours, starts to talk with you about the dispute. May you discuss the matter with your non-lawyer friend?
- Your company is under investigation by a grand jury. You are told that prosecutors have been contacting employees at home and questioning them about matters related to the case. Is the government allowed to do this?
- Your company is suing another company. A disgruntled ex-employee of the other company calls you and offers juicy testimony. Can you listen?

General Principles

ABA Model Rule 4.2 provides: "In representing a client, a lawyer shall not communicate about the subject of the representation with a person the lawyer knows to be represented by another lawyer in the matter, unless the lawyer has the consent of the other lawyer or is authorized by law to do so." In jurisdictions following the ABA Model Code of Professional Responsibility, essentially the same rule is in DR 7-104(A)(1).

If a corporation is represented by an attorney in a matter, corporate employees who meet certain characteristics are considered "represented persons" and are off limits to opposing counsel. *See Orlowski v. Dominick's Finer Foods, Inc.*, 937 F. Supp. 723 (N.D. Ill. 1996). The employees who may not be contacted are as follows:

- Employees who have "managerial responsibility" in the organization.
- Employees whose acts or omissions relating to the matter in litigation may be imputed to the organization for purposes of liability.
- Employees whose statements may constitute admissions on the part of the organization.

Thus, in the first example above, Rule 4.2 would likely prohibit an informal conversation with a senior official of your adversary. *See Carter-Herman v. Philadelphia*, 897 F. Supp. 899 (E.D. Pa. 1995). He or she has managerial responsibility. Also, his or her acts or omissions relating to the case might be imputed to the organization, and his or her statements might constitute admissions on the part of the corporation. A caveat: the exact description of the employees who are off-limits varies widely from jurisdiction to jurisdiction. Contacts forbidden in some jurisdictions are permitted in others. For example, New York allows contacts somewhat more expansively than other jurisdictions. *Niesig v. Team I*, 76 N.Y.2d 363 (1990).

It is no defense to a violation of the rule that the lawyer did not initiate the prohibited conversation. It is the lawyer's responsibility to be aware of the rule and to comply with it.

The Criminal Context

In criminal cases, prosecutors have more freedom to contact corporate employees than private attorneys have in the civil arena. A number of courts have held that prosecutors may contact an employee of a represented company during the investigative stage of proceedings, before indictment, even if the employee would be off limits under the Rule 4.2 standards. One rationale is that the government's interest in investigating crime outweighs the interests protected by Rule 4.2. *United States v. Balter*, 91 F.3d 427 (3d Cir. 1996) (collecting cases).

Thus, in the second example given above, many jurisdictions would permit prosecutors to contact employees during the preindictment stage of an investigation of a corporation even if, for example, the employee had managerial responsibility. In recent years, however, some courts have retreated from this position, imposing restrictions on preindictment contacts by the government. *United States v. Talao*, 222 F.3d 1133, 1139 (9th Cir. 2000); *see also United States* ex rel. *O'Keefe v. McDonnell Douglas*, 961 F. Supp. 1288 (E.D. Mo. 1997), *aff'd* 132 F.3d 1252 (8th Cir. 1998).

Throughout the 1990s, the Department of Justice ("DOJ") took an absolutist position in this debate. DOJ argued that its lawyers were not bound by state ethics rules, such as Rule 4.2. DOJ went so far as to promulgate regulations that would have allowed it to contact represented persons freely. Congress, however, disagreed with DOJ's view and passed legislation providing that "[a]n attorney for the Government shall be subject to State laws and rules, and local Federal court rules, governing attorneys in each State where such attorney engages in that attorney's duties, to the same extent and in the same manner as other attorneys in that State." 28 U.S.C. § 530(B) (1998). This new statute will operate to limit contacts by government prosecutors with represented persons, but not eliminate them altogether because, in some jurisdictions, Rule 4.2 is interpreted to permit such contacts in some circumstances.

Former Employees

Former employees of a represented corporation enjoy the lowest level of protection under Rule 4.2. They are generally considered available for interview by all parties to litigation. *See* ABA Formal Op. 91-359 (1991); *Wright v. Group Health Hosp.*, 691 P.2d 564 (Wash. 1984). They are not considered "represented persons" under the rule because they no longer work for the corporation that has retained counsel. Thus, in the third example provided above, you may take the call from the ex-employee. Be careful if the ex-employee is a former attorney or if he or she tries to reveal attorney-client confidences or attorney work product–these topics are off limits although conversation about nonprivileged subjects may occur. Also keep in mind that a few jurisdictions limit contacts with high-ranking employees after they have left the corporation. As always, check the law of the relevant jurisdiction closely.

Conclusion

It pays to proceed with caution in this area. Mistakes can cost lawyers and clients. Being aware of the intricacies of Rule 4.2 can help a lawyer to take advantage of the mistakes of the other side–and to avoid those same embarrassing and damaging mistakes. ■

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Walking the Voluntary Disclosure Tightrope

*by Roger C. Spaeder**

It is every in-house lawyer's nightmare. Following disclosure to federal authorities of your company's noncompliance with laws or regulations, you receive word that, while your company has been admitted to a government-sponsored voluntary disclosure program, one of your senior managers has been designated a target of the criminal investigation triggered by your disclosure. You now confront the dilemma of completing settlement negotiations with the Department of Justice ("DOJ") while dealing with an anxious executive who does not want to be thrown to the wolves.

How should the targeted executive be treated by the company during its efforts to obtain favorable treatment from the government? What options are open to the company that will allow it to assist its employee without appearing to tolerate or reward alleged criminality? This tension is particularly acute in high-risk industries, such as healthcare, pharmaceuticals, government contracting, securities, and banking, where the risk of administrative exclusion is catastrophic.

An essential theme in every voluntary disclosure program is that the company will settle its dispute by "cooperating" in the broadest sense, which often means disengaging from the accused executive. Because that individual may be a tenured and loyal officer of the company and because the required showing of cooperation may occur long before he or she has been convicted of any crime, in-house counsel must find a solution that is at once satisfactory to the government and fair to the employee.

Although the company must take some action with respect to the accused employee to demonstrate cooperation, a variety of options are available that are, to varying degrees, fair to the employee while addressing concerns of the government.

Transfer to a nonregulated function or subsidiary. The government has a legitimate interest in seeing that the targeted employee stops performing the function that gave rise to the alleged violation. For example, removal of such an employee from direct sales contacts with government customers (in a gratuity investigation) or a transfer from the military to civilian manufacturing component (in a defective testing investigation) usually suffices to elim-

inate the government's concern about future violations.

Administrative leave pending conclusion of trial. It may be necessary to remove the employee completely from the line of fire pending trial by affording him administrative leave with pay. The personnel policies of some companies allow such action during the course of a job-related investigation without loss of position or compensation. Such protections are more common in government employment than in the private sector, but consideration should be given to this option even if not formally recognized by company policy.

Consultancy relationship pending trial. Given the government's insistence on cooperation, it may not be feasible to retain the executive as a direct employee pending his criminal trial. Other considerations, such as securities laws reporting requirements for officers and directors, may make it difficult to retain an indicted employee on the payroll. A paid consultancy for the executive may represent a satisfactory compromise because it removes the former employee from direct involvement in company activities while maintaining some relationship.

Resignation, severance, and outplacement. When termination of the employee's relationship with the company is unavoidable, it may still be appropriate to offer the executive a severance package and outplacement assistance. The prosecutor may grumble that a departing employee should not be "rewarded" for alleged misdeeds, but few corporate dispositions are derailed because the board of directors negotiates a severance agreement with the employee.

The remaining question is whether the company may claim the benefits of cooperation while funding an employee's criminal defense. Under the laws of most states, a board of directors is permitted to advance attorneys' fees for the defense of an indicted employee on a certification by the employee of his good faith belief that his conduct was in the best interests of the company. In some jurisdictions, the employee may be required to execute a promise of repayment in the event he is ultimately determined not to have been entitled to advancement.

The availability of legal fees is indispensable to an indicted corporate employee seeking vindication at trial. By the same token, federal prosecutors have long appreciated the tactical value of denying the defendant well-funded representation.

The official Justice Department policy on corporate prosecutions sets forth the general principle that "[i]n 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." The commentary to this principle includes the following:

> . . . 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, 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 the value of a corporation's cooperation. . . "

Federal Prosecution of Corporations, § VI, ¶ A (June 16, 1999).

The commentary notes that "[s]ome states require corporations to pay the legal fees of officers under investigation prior to a formal determination of guilt. Obviously, a corporation's compliance with governing law should not be considered a failure to cooperate." (*Id.*, fn. 3.) Unfortunately, very few states "require" the advancement of legal fees before a formal determination of guilt, but rather authorize the corporation, consistent with its bylaws, to pay legal fees upon submission of an affidavit of good faith by the employee. The official DOJ policy, therefore, does not definitively resolve whether the company may advance its employee's legal fees.

Ultimately, the issue must be resolved in case-by-case negotiations with the prosecutor, mindful that it is rarely in the long-term interest of the company to throw its employee overboard without a lifeboat. ■

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Zuckerman Spaeder

Zuckerman Spaeder is a multi-practice firm of more than 70 lawyers in Washington, Baltimore, New York, Miami, Tampa and Wilmington. Major practice areas include complex civil and commercial litigation, government investigations, criminal and regulatory proceedings, bankruptcy, real estate and corporate law.

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Zuckerman Spaeder attorneys represent companies and executives in many industries who are targets, subjects and witnesses in all phases of investigations. We assist companies in responding to state and federal regulatory and criminal investigations, in subpoena compliance, and, when necessary, we conduct internal investigations. We design and implement compliance programs and other measures to prevent misconduct and facilitate self-reporting. We craft strategies to negotiate satisfactory resolutions with prosecutors and regulators and mount comprehensive vigorous defenses at trial or on appeal.

Our clients includes hospitals, nursing homes, and other health care organizations who face fraud and abuse claims, alleged violations of anti-kickback laws, and other claims of misconduct. We defend financial services firms and their executives against allegations of securities fraud, insider trading and market manipulations, and we represent companies and executives alleged to have engaged in price-fixing and other antitrust offenses. We assist clients suspected of government procurement fraud, defending against the underlying allegations and designing resolutions to avert threatened suspension and debarment.

The firm has represented White House and cabinet officials, members of Congress, and other senior government officials in independent counsel and congressional investigations and against various criminal charges. In addition, the firm's federal election law specialists counsel organizations on the formation of political action committees and participation in the political process, and defend those accused of violating election laws.

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