

## White-Collar Crime

### *Counseling Corporate Clients Under Investigation*

BY LORETTA E. LYNCH

**I**N TODAY'S enforcement environment, it is more likely than ever that the corporate client may become embroiled in a criminal investigation. White-collar crime has been placed on the national law enforcement agenda by legislators and prosecutors. The increased law enforcement and regulatory scrutiny will not be solely limited to "household name" entities, but will take into account the entire corporate landscape. This scrutiny is likely to come not just from federal and state prosecutors but also from the Securities and Exchange Commission and NASD.<sup>1</sup>

Upon learning that a client is the subject or the target of a criminal investigation, it is vital that certain steps be undertaken quickly. An important new part of the law enforcement landscape, the Sarbanes-Oxley Act and the SEC rules promulgated thereunder, impose investigative and reporting requirements on corporate counsel who learn of allegations of violations of the securities laws, breach of fiduciary duty or violations of similar state and federal laws. While the investigative obligations are not inconsistent with prior practice of many white-collar practitioners, counsel must now be aware of the internal management and committee reporting requirements imposed by law.<sup>2</sup>

At the outset, counsel must learn as much as possible about the matter so that a plan of action for responding can be

devised. These steps include preparing to respond to government subpoenas and requests for interviews, conducting an internal investigation, and discussions with the government to learn as much as possible about the nature and scope of the investigation. If the client is a publicly traded company, counsel must also ensure that disclosure obligations are met, as well as make arrangements to deal with the press should the investigation become public knowledge.

A primary goal in corporate representation is avoiding indictment, which can have significant ramifications beyond the penalties of probation and fine, including debarment from certain government programs and aiding greatly the ensuing wave of civil litigation. If, at the end of the investigation indictment cannot be avoided, counsel should, through negotiations with the government, attempt to limit the scope of charges brought as much as possible to a discrete portion of the company, if the illegal activity can be so confined.

In corporate representations, counsel must also continually assess their ability to represent members of management and other employees as the investigation progresses. Conflicts of interest may arise that will require an objective recommendation of separate counsel for certain individual actors. Outside counsel experienced in criminal investigations can be an invaluable resource, both for assessing the scope of the criminal investigation as well as managing the myriad internal issues that will arise.

grand jury subpoena, in whatever form they exist, leaves the client open to criminal contempt and obstruction of justice charges, as does failure to preserve documents from destruction once the fact of investigation is known.<sup>3</sup>

A memo or e-mail must be sent to all employees in the areas that have documents and materials responsive to the subpoena. This memo should outline the subject matter of the requested information, generally by including a copy of the language from the subpoena, and clearly direct that nothing in the relevant categories be destroyed or deleted until further notice. In addition, steps must be taken to identify all possible locations for data to avoid even the appearance of non-compliance. This will require consultation with management as well as the IT department.

The standard document retention policy must be immediately suspended until further notice. All shredding of materials related to the relevant matters must be suspended, and arrangements made for storage of the material. Automatic e-mail deletion programs must also be suspended, and back-up tapes preserved. Some computer systems use back-up tapes that are automatically re-used, effectively recording over material. This program must be suspended as well, and arrangements made to store the tapes and subsequent ones used. Finally, counsel should be the point of contact for questions that may arise under these directions.

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#### **Document Production**

The area of document production, particularly of electronic media, contains many pitfalls for the practitioner. Failure to provide documents responsive to a

#### **Employee Interviews**

In addition to advising employees to preserve all documents, counsel should identify the employees who are knowledgeable about or work within the rele-

vant area. These are also the employees most likely to be approached by the government for interviews. Counsel should advise employees that they might be contacted by the government for interviews.

Counsel should inform employees of their right to decline an interview or to proceed, of the availability of counsel, and of the need to be absolutely truthful should they choose to speak with investigators. Counsel should not direct employees not to consent to government interviews, even by inference. This will be construed by the government as obstruction of justice or impeding its investigation, and significantly reduce the value accorded to any subsequent efforts to cooperate.

### **Internal Investigation**

Counsel should conduct an internal investigation of the issues raised as soon as is practicable. This will both educate counsel about the matter and identify areas of criminal liability. In addition, pinpointing criminal activity early on can give the company the opportunity to change practices, remove personnel and cooperate early in the investigation, which are all important factors in avoiding indictment or other sanctions.

Outside counsel, preferably with experience in white-collar matters, should be retained to handle the internal investigation, which must be seen as independent and objective. Through the use of outside counsel the company gains the benefit of counsel with specific expertise, and of counsel that is not perceived to be aligned with management. This becomes particularly useful should management prove to be involved in wrongdoing. The internal investigation will involve gathering and reviewing materials produced to the government, as well as interviews of the employees connected to the subject matters under investigation. Depending upon the nature and complexity of the subject matter, counsel may need to retain additional professionals to assist in the investigation, such as forensic accountants.

During employee interviews, outside counsel must notify the employees that

they represent the company, and not the individual employee. They should also inform the employee that the privilege pertaining to the conversation belongs to the company, which will have the ultimate decision in whether it is ever waived. Employees should be instructed not to discuss their interviews with others. Witnesses outside the company, e.g., customers, may need to be interviewed as well.

The company's compliance program designed to address the issues under investigation must be reviewed. If there is no compliance program, one must be instituted. If the current compliance program fails to either prevent wrongdoing or to alert management to the problems, it may have to be revised. The Department of Justice carefully scrutinizes the nature and effectiveness of compliance programs in making charging decisions as well as sentencing recommendations. While the presence of a compliance program will not, by itself, prevent criminal charges, its absence will guarantee a harsher review and, should a corporate plea be necessary, prevent the company from gaining important mitigation points at sentencing.<sup>4</sup>

If wrongdoing is uncovered by the internal investigation, it must be dealt with immediately. Any illegal activity must cease, and wrongdoers must receive discipline. Sanctions, demotion or termination may be called for. Counsel must determine what remedial actions need to be taken, if any, such as restatement of prior earnings or restitution. Wrongdoing must also be reported to the government. In the newly revised Principles of Federal Prosecution, the U.S. Department of Justice makes clear that failure to promptly report illegal conduct will be construed as impeding the government's investigation, and weigh against the argument that a company is cooperating fully.<sup>5</sup> In addition, failure to promptly disclose illegal conduct can deprive the corporate client of valuable mitigation points at sentencing.<sup>6</sup>

### **Initial Inquiries**

Experienced counsel should speak with

the prosecutor handling the investigation soon after learning of its existence. At the outset, counsel must determine whether the client is a subject or target of the investigation, or a witness in the matter. Inquire as to the subject matter of the investigation, and the nature of any evidence implicating the client. Learning the prosecutor's view of the client is essential in formulating strategy for dealing with the investigation.

In the initial contact, counsel should try to narrow the breadth of any grand jury or administrative subpoenas that have been received. Often the government drafts both the location and subject matter of subpoenas for documents very broadly. The prosecutor is likely to agree to narrow the scope and volume of documents to be produced, if the overbroad nature of the requests can be outlined to her, in light of her description of the investigation. The prosecutor will generally agree to suspend production of materials not immediately germane. These materials must still be preserved, but such an agreement considerably lessens the burden of production. Counsel should advise the prosecutor that, unless notified of a conflict of interest, they represent the company and its officers, and ask that all requests for interviews go through counsel.

In dealing with the government, many of the practices that have become second nature in civil litigation, e.g., delays in document production, hostility between attorneys, are counterproductive in the extreme in criminal investigations.

### **Cooperation in Investigation**

Even in the absence of clear evidence of wrongdoing from an internal investigation, the corporate client must decide, fairly early on, whether to cooperate with the government investigation.

As a rule, the government encourages cooperation, and will give great weight to the nature and completeness of cooperation in making final charging decisions. Counsel must be aware, however, of the government's recently expanded view of what constitutes complete cooperation. Recently revised Department of Justice

Guidelines for Corporate Prosecution, issued in January 2003, stress the weight that will be given to, inter alia, waiver of the work product privilege and disclosure of the results of internal investigations.<sup>7</sup> Counsel must be aware of the potential for this waiver to be construed as extending to other agencies and third parties, including civil litigants.

Should the decision be made to cooperate and provide the results of an internal investigation or any other privileged material, counsel should negotiate with the prosecutor a written confidentiality agreement, wherein the government agrees to maintain confidentiality of the materials provided, and the disclosure pursuant to the agreement does not constitute a waiver of the attorney client and work product privilege as to any other entity. Such agreements are becoming more commonplace. In general, judicial treatment of confidentiality agreements can vary from jurisdiction to jurisdiction.<sup>8</sup> New York courts have upheld such agreements, however, and they should be pursued with the prosecutor.<sup>9</sup> The SEC and NASD also give great weight to a company's decision to waive privilege and turn over the results of an internal investigation in making charging and sanctions decisions.<sup>10</sup>

In addition to looking at affirmative efforts to cooperate, the Department of Justice will look closely at behavior deemed to impede its investigation, such as incomplete or delayed document production, and directions to employees not to cooperate. The department also scrutinizes corporate behavior carefully to determine if the company appears to be shielding culpable employees, e.g., by providing attorney's fees in the absence of a legal requirement to do so, or failing to sanction culpable employees.<sup>11</sup> These issues heighten the necessity of disciplining such employees, as outlined above.

## Counseling the Client

Perhaps the most difficult part of counseling a client under investigation

can be convincing that client of the potential for criminal liability arising out of what they may have rationalized as aggressive business practices. Clients often convince themselves they have "done nothing wrong," or at worst committed only a "technical violation." Once counsel has determined the nature of the investigation and any allegations involving the client, counsel must assess whether there is any factual basis for liability. The client must be advised of the nature of any charges that could be brought, as well as be provided with an assessment of the strength of any such case. Familiarity with government investigations is crucial in this regard.

Even though the department's guidelines for corporate prosecution still discuss the issues of the collateral consequences of corporate prosecution and the availability of non-criminal sanctions, these factors generally receive much less weight than those involving the nature of the crime and the nature of any cooperation. The client must realize that his perception of the evidence will not control the decision whether or not to prosecute. Further, even if the initial allegation of the investigation ultimately cannot be sustained, the government will look closely at any behavior during the investigation that could be construed as obstruction of justice.

The client should also be advised of the business disruption and added stress a criminal investigation brings into the workplace. The lack of control that businesses have over the pace and scope of a criminal investigation is often a great source of frustration for management.

## Conclusion

Being the subject or target of a criminal investigation is a lengthy, frustrating and costly process for the corporate client. There are, nevertheless, steps that can be taken to present the company in the best possible light to the government so that the ultimate decision on how to proceed is informed by the company's best efforts.

(1) The legal standard governing the liability of a corporate entity for the criminal conduct of its agents is well settled. The courts have long held that a corporation is criminally liable for the illegal acts of its agents only if the government can establish that (i) the corporate agent was acting within the scope of his employment, and (ii) the agent's actions were intended, at least in part, to benefit the corporation. See *New York Central & Hudson River RR. v. United States*, 212 U.S. 481, 493-94 (1909) (upholding the constitutionality of corporate criminal liability as an extension of principles governing civil liability, which impute the act of a corporate agent to the principal when "the act is done for the benefit of the principal, while the agent is acting within the scope of his employment"); *United States v. Koppers Co.*, 652 F.2d 290, 298 (2d Cir. 1981) (upholding jury charge which instructed jury that to hold corporation criminally liable for the acts of its managerial agents, jury must find that acts were "done on behalf of and to the benefit of the corporation and directly related to the performance of the duties the employee has authority to perform"); *United States v. Jacques Dessange, Inc.*, 103 F.Supp.2d 701, 706 (S.D.N.Y. 2000) (conviction of corporate defendant will stand where evidence is sufficient to permit jury to conclude "beyond a reasonable doubt that a supervisory employee's actions 'were for the benefit of and authorized by' the company") (citation omitted).

(2) 15 U.S.C. §7201 et seq.; 17 C.F.R. §205 (2003).

(3) Increasingly, the government will also proceed by way of a search warrant to obtain computers and documents. Cautious corporate counsel will appoint a crisis management team beforehand to defend in connection with a warrant.

(4) U.S. Sentencing Commission, Guidelines Manual §8A1.2, comment (n.3 k) (November 1997); see also USSG §8C2.5(f).

(5) Memorandum from Deputy Attorney General Larry D. Thompson re Principles of Federal Prosecution of Business Organizations, Jan. 20, 2003 (Thompson Memorandum).

(6) USSG 8C2.5(f); USSG 8C2.5(g).

(7) Thompson Memorandum.

(8) Morvillo and Anello, "Waiver Issues in Corporate Investigations," *New York Law Journal* June 2, 2003.

(9) See, *Maruzen Co. Ltd. v. HSBC USA Inc.*, 2002 WL 1628782 (SDNY July 23, 2002).

(10) Securities and Exchange Act of 1934 Release No. 44969, Oct. 23, 2001; NASD Sanctions Guidelines: Principal Considerations In Determining Sanctions.

(11) Thompson Memo.

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