

Rethinking Corporate Cooperation

By Jim Walden and Farrah Pepper

In the post-Enron world, many public companies have come under intense scrutiny from the government. A diverse chorus of critics argues that the Department of Justice (DOJ) has gone too far, citing the overzealousness of line-level prosecutors, their failure to adhere to the measured tone struck by higher-level officials in their public pronouncements, and their general tendency to treat companies as racketeering organizations.

Aggressive prosecutors need not instill fear in a company or its counsel. Pushback — politely delivered and judiciously selected — is appropriate (and often required) during governmental investigations of alleged corporate wrongdoing. Taking an *über*-aggressive prosecutor “up the line” to supervisory personnel is sometimes a necessity, and often well received. Even if the prosecutors do not like it, corporate directors and their counsel are duty bound to prevent the government from running roughshod over the company, even during a criminal investigation. In other words, companies should not feel “forced” to abide aggressive demands. As time has shown,

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DOJ’s bark is often worse than its bite.

DESPERATE TIMES? DESPERATE MEASURES

Much has been written about DOJ’s policies and practices for investigation of corporate crime, and, in particular, the 2003 memo issued by then-Deputy Attorney General Larry Thompson. The Thompson Memo has become well known, for better or worse, in boardrooms across the globe. Under the white light of governmental investigations, lawyers regularly advise companies to satisfy any government demand in order to prove the company’s good faith. The cost of anything short of complete cooperation is usually deemed too high.

Government demands have become more aggressive and often are delivered in blunt or shrill language. Most lawyers representing public companies have personal horror stories of prosecutors who:

- demanded blanket waivers of the attorney-client and work product privileges, even at the start of an investigation — long before wrongdoing was clearly identified, let alone proved;
- urged the termination of executives even before any indictments were filed;
- prevented companies from advancing legal fees to executives under investigation;
- stopped company counsel from providing information and even documents to counsel for individual executives;
- demanded that company counsel refrain from interviewing current and former employees; and
- required companies to refrain from making any public statement that contradicts the government’s theory of liability.

Commentators and practitioners have complained that, under these circum-

stances, companies are “forced” to abide abusive government demands, lest they be indicted and suffer the “corporate death penalty.” This position is often punctuated by the tale of Arthur Andersen’s indictment, trial, and demise. A virtual cottage industry of bar associations, trade groups, and pundits has emerged, urging that the federal government has gone too far, and that Congress should intercede to move the pendulum back.

In fact, DOJ is now bracing for legislation that may curb its authority to conduct corporate investigations under the principles of the Thompson Memo. Proposals have included statutory modification to prosecutorial discretion, model jury instructions to limit corporate liability, and Congressional action to change standards for corporate liability.

‘COOPERATION’ DOES NOT MEAN CAPITULATION

Demanding prosecutors are more often motivated by uncertainty than blood lust. They fear that company counsel will always portray wrongful conduct as negligence or recklessness rather than intentional wrongdoing. They fear that companies will hide knowledge of wrongdoing behind attorney-client privilege. Fear of such manipulation is apparent even in public remarks by DOJ officials. One recently said: “Some attorneys assert the privilege like the famous scene of Lucille Ball gobbling chocolates off a conveyor belt. Everything is swallowed up by in-house legal counsel.” This exaggerated analogy is symptomatic of DOJ’s broad perception that companies and their lawyers seek to hinder or obstruct prosecution.

Despite hard-line statements by some DOJ officials and line-crossing by some

field-level prosecutors, the government has not haphazardly sought indictment of “uncooperative” companies. Instead, it has relied heavily on pretrial diversion programs for the overwhelming majority of accused companies, including the most notorious violators. Even in the Computer Associates case, where the government proved a 2-year conspiracy among senior management to obstruct the government’s investigation, the company received the benefit of a deferred-prosecution agreement.

Those who claim that unflinching capitulation is required for corporate cooperation to be “genuine” argue from a false premise: that every instance of pushback risks indictment. If a company, cooperating in good faith, helps the government find wrongdoers, prosecutors can have little complaint about the company’s resisting some requests. Most government attorneys remain reasonable in making demands on companies during the course of investigations. Most make aggressive initial demands — like any lawyer entering a negotiation — but remain open to moderation if approached in good faith. Most allow a company to conduct a complete investigation under its own terms. Most place no restrictions on payment by the company for individuals’ attorneys’ fees. Most are open to negotiation over the scope of privilege waivers. Of the very few corporate indictments filed since Enron, not a single one was based on a company’s decision to resist some of the government’s demands.

CONTEXT IS EVERYTHING

Resisting government demands that hinder a company’s ability to gather facts is imperative in these times. In many recent prosecutions, the government has been unable to prove its case against companies and high-level executives. Just last month, a federal jury in San Francisco acquitted former McKesson executives in an accounting scandal. In October, federal prosecutors dropped charges against a trader from Fleet Specialists, after dropping similar charges against another trader in September. In August, federal prosecutors dismissed obstruction-of-justice charges against Frank Quattrone. Acquittals, dismissals, or hung juries resulted from prosecutions against executives of PurchasePro, Tyco, Duke Energy, Bank of America, CIBC, and Symbol Technologies, just to name a

few, and the prosecution of Tenet HealthSystems faced similar collapse.

The government attributes these failures to jury confusion, but a better explanation rests in the government’s penchant for “gaming” criminal theories. When prosecutors find no statute directly prohibiting conduct they view as wrongful, they construct a novel theory of liability. Theory gaming—a form of manipulation to stretch criminal statutes—has been behind spectacular failures in a number of recent prosecutions. The Tenet HealthSystems prosecution and the Nigerian-barge prosecution of Merrill Lynch employees are prominent recent examples.

With this background, it is a mistake to roll over too quickly to a belligerent prosecutor. Sometimes, young and ambitious prosecutors first look for bad facts and then seek a theory to fit them. All too often, they do not look for exculpatory evidence and ignore the context of conduct they deem nefarious. If the company and its lawyers yield to unreasonable requests—such as refraining from interviewing its own employees, withholding documents and information to counsel for individual executives, and agreeing not to contradict the government’s questionable theory—fiduciary duties are left in the dust. The Thompson Memo does not require such capitulation.

A DUTY TO IMPOSE LIMITS ON COOPERATION?

To borrow an evocative phrase from the Delaware Supreme Court in *Malone v. Brincat*, the “constant compass” guiding all actions taken by directors is fiduciary duty, which includes duties of care, loyalty, and good faith. Taken together, these duties require that the directors act in a fully informed manner, act in the best interests of the corporation and shareholders, and act honestly and faithfully to their obligations to the company.

Though a policy of blanket “cooperation” might sound reasonable in a vacuum, it is not always the best course for a company. If the government demands a blanket privilege waiver, most courts will hold the privilege waived in follow-on civil litigation. If companies yield to government demands to refrain from interviewing their own employees, any exculpatory information they may have is lost to the company. If a company cuts off advancement of

attorneys’ fees, it may have severe problems recruiting talented executives in the future.

These collateral consequences should give directors serious pause. Looking beyond the immediate investigation to the future health of the company, they should weigh the long-term risks and benefits of each new government demand, including the possible consequences of resisting. They should not underestimate their need to have every pertinent fact, including exculpatory evidence (even if prosecutors are uninterested in such information). Directors cannot simply fold under pressure and abdicate any further responsibility for the concessions their lawyers ultimately make to the government. Prosecutors, who are quick to criticize any lack of director diligence during the period of alleged misconduct, should expect directors and company counsel to assess the long-term impact of intrusive and sometimes destructive government demands. Despite noises prosecutors make to the contrary, they generally understand and respect these assessments and are willing to entertain responsible proposals to accommodate the exercise of the board’s duties.

CONCLUSION

Companies don’t need to capitulate to hard-nosed requests and unprofessional conduct by governmental attorneys. Lawyers representing corporate targets, and board members deciding the scope of cooperation, should not miss the forest for the trees. Pushback is allowed and sometimes required. The polite but firm setting of limits on a company’s eagerness to please the government is not likely to result in indictment and all its attendant consequences.



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