

White Collar Criminal Defense, Regulatory Compliance and Special Investigations Update

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United States Sentencing Commission Issues Proposed Guidelines Related to the Sentencing of Companies Charged With Federal Crimes

**Hi, I am from the government and I am here to help you
[By undermining your ability to govern your own company]"**

Last month, the United States Sentencing Commission ("USSC") proposed several modifications to the United States Sentencing Guidelines that will have far-reaching ramifications for any company caught up in a federal investigation. The amendments related to (1) steps a company should take if it uncovers criminal conduct, (2) document retention policies, (3) possible installation of corporate monitors, and (4) corporate governance issues related to compliance.

Let's discuss the most controversial topic first: corporate monitors. The USSC has proposed an amendment to Section 8D1.4, which governs conditions of probation for organizations. The amendment modifies the USSC's "recommended conditions of probation" by stating that the company "shall be required" to retain an independent corporate monitor, agreed upon by the parties or appointed by the court. Further, the scope of the independent monitor's role is to be approved by the court, and the organization is to pay for the monitor's compensation and costs.

Historically, monitors have been installed in organizations where the courts had no confidence that the organization would police itself in order to be sure the criminal conduct would not repeat. Several workers unions in the New York and New Jersey area were required to install monitors in the 1980's. More recently, monitors have been used in some prosecutions. Most notably, five major medical device companies were required to install monitors as a condition of settling cases brought by the United States Attorney's Office in New Jersey.

This Amendment goes much further. It announces a policy statement encouraging the courts to impose a monitor for every company where probation is imposed. The monitor has the power to conduct unannounced examinations of the company's books, records and "facilities subject to probation supervision," and the monitor can force the company to submit to "interrogation of knowledgeable individuals within the organization." This is an incredible expansion of the use of monitors.

In essence, these provisions mean that any and every company that has one lapse with a rogue employee and is charged and sentenced to probation, will face the possibility of having an

expensive "in-house cop," who will have virtually unfettered power to wreak havoc in the corporate governance of the company (and has a financial incentive to do so). Indeed, we have already seen such abuse in the past use of monitors. As was widely reported in 1996, when Bristol Myers was under the supervision of a monitor, the United States Attorney who had appointed the monitor actually attended a Board of Directors meeting regarding the ouster of Bristol Myers' then CEO. That is "monitoring" a bit far afield from any past misconduct allegedly committed by Bristol Myers. We also know from past history that these monitors are ridiculously expensive. As noted above, in 2007, five medical device companies were required to employ monitors selected by the prosecutor as a condition of settling criminal and civil charges with the United States Attorney's Office in New Jersey. Former Attorney General John Ashcroft was appointed as monitor for one of the companies. That company later reported in an SEC filing that Mr. Ashcroft and his firm would receive as compensation from the corporation between \$28 and \$52 million under an 18-month agreement.

The use of these monitors is just plain ol' overkill. Not every corporation on probation warrants the imposition of a disruptive and expensive monitor. All other defendants on probation from bank robbers to embezzlers are allowed to self-police themselves under the supervision of a probation officer. That is what the current system allows for corporations, and it should stay that way. Monitors should only be imposed in the most extreme circumstances where the government can meet its burden of showing that the company is not policing itself and is, therefore, very likely to break the law again.

The other proposed amendments to the Sentencing Guidelines are far less controversial. In fact, for the most part, they are similar to the "best practices" that we often advise clients to undertake both before and after misconduct is uncovered at the company.

The first of those amendments speaks to the policies of document retention. The amendment seeks to add a section to Section 8B2.1 titled "Effective Compliance and Ethics Program" (the "Compliance Guidelines"), which guides effective corporate compliance programs. The amendment provides that both "high-level personnel" and "substantial authority personnel" (*e.g.*, the executive management and members of the Board of Directors) must be aware of the organization's document-retention policies and conform such policies to the objective of an effective compliance plan. In addition, as part of a periodic assessment of its compliance plan, the organization will be required to verify that all employees are aware of the document-retention policies, and that such policies advance effective compliance.

Another amendment addresses the procedures a company must undertake when it becomes aware of misconduct. The amendment outlines steps such as self-reporting, cooperating with authorities, providing restitution and remediation to identifiable victims, and periodically modifying its corporate compliance as necessary. Specifically, the amendment states that the company "may take the additional step" of employing an independent monitor to oversee the necessary modifications. Again, this is another instance of the Sentencing Guidelines encouraging the use of monitors, but at least in this situation, it appears that the company has reasonable latitude to decide if it is prudent to employ a monitor. This would allow the company to have some control over the scope and cost of the monitor's work.

Finally, USSC issued for comment the question: Should the Sentencing Guidelines be amended to provide a reduction in sentencing for an effective compliance program even when executive officers, directors and individuals with a substantial ownership interest are involved in the wrongdoing if (1) the individual(s) with operational responsibility for compliance report directly to board level (*e.g.*, an audit committee of the board of directors), (2) the compliance program was successful in detecting the offense prior to discovery, and (3) the organization promptly reported the criminal conduct to the appropriate authorities?

This could prove to be a very helpful provision for companies. Currently, sentence reductions are not available to organizations that have an effective compliance program if executive officers or directors are the wrongdoers. With this issue for comment, the USSC seems to be opening the door to allow some reduction at sentencing if the company can show its ethics and compliance officers report to the Board of Directors and not some individual employee or officer. This amendment follows recent best practices in compliance and governance and seems to be the USSC's push to prompt companies to give the Special Committees of the Board and the high-ranking compliance officers assigned to root out misconduct the ability and encouragement to follow the evidence wherever it leads and to report such misconduct to the Board without fear of reprisal (or pressure to cover up the misdeeds) by any self-interested and perhaps culpable officers or employees.

To summarize, the amendments related to use of the monitors are a bad idea (and will be vehemently opposed by the white collar bar and the business community at the hearings to be held this month). The remaining amendments actually outline many best practices we counsel for all clients. In that regard, we stand ready to help insulate your company from exposure by first completing an organizational risk assessment, and then developing policies and training modules on your ethics and compliance policies, including policies with regards to document retention.

For more information, please contact the White Collar Criminal Defense, Regulatory Compliance and Special Investigations Practice Group at Lane Powell:

206.223.7000 Seattle
503.778.2100 Portland
whitecollar@lanepowell.com
www.lanepowell.com

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