Whistleblowing incentives for lawyers?
Second Circuit weighs whether conflict-of-interest rules bar attorneys from suing ex-employers under False Claims Act

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Corporate-insider whistleblowers have been awarded more than $3 billion in lawsuits against companies for defrauding the government. By filing lawsuits in the name of the government under the Civil War-era False Claims Act, these qui tam whistleblowers (called "relators" under the statute) can recover up to 30 percent of the proceeds. This powerful financial incentive has enabled the government to recover more than $20 billion from health care companies and government contractors that committed fraud.

Should lawyers-like other corporate insiders-be able to take advantage of these financial incentives for blowing the whistle on corporate fraud? That is the question that the U.S. Court of Appeals for the Second Circuit wrestled with on August 23 at an oral argument in U.S. ex rel. Fair Laboratory Practices Associates v. Quest Diagnostics.

Judicial precedents favor the whistleblowing lawyers, and new U.S. Securities and Exchange Commission (SEC) regulations may inspire more lawyers to seek financial incentives for blowing the whistle on their clients.

The Second Circuit case involves Mark Bibi, who was general counsel of a health care diagnostic testing company. When Bibi became concerned that the company's billing practices violated the federal criminal anti-kickback statute, he sought an opinion from outside counsel and raised his concerns with the company's management and three members of its five member board. Despite Bibi's concerns, the company continued these practices. After Bibi left the company, he learned that Quest Diagnostics (which had purchased his former employer in 2003) also used these same billing practices. Five years after leaving the company, Bibi joined two other former managers in becoming relators and suing their former employer and its parent, Quest, under the False Claims Act.

After the defendants realized that Bibi-a lawyer-was one of the relators, they asked the district court to dismiss the lawsuit, arguing that Bibi revealed client confidences and violated the subsequent conflict-of-interest rule. The district court agreed, dismissing the entire case. Bibi and the other relators are asking the Second Circuit to revive the lawsuit.

New York bar rules allow lawyers to reveal information "to the extent the lawyer reasonably believes necessary...to prevent the client from committing a crime." N.Y. Rule of Professional Conduct 1.6(b). Bibi believed that his former client was violating the anti-kickback statute and that disclosing this information by filing the False Claims Act lawsuit was necessary to prevent this ongoing crime. As long as the lawyer is revealing information subject to a confidentiality exception, he argues, he should be able to take advantage of whistleblower financial incentives.

The weight of precedent is on Bibi's side. Three other courts have examined this issue and ruled that lawyers may file False Claims Act lawsuits against former clients as long as the information they reveal falls into an exception to their confidentiality obligation. One court even said that lawyers "should be encouraged" to file such lawsuits. U.S. ex rel. Doe v. X Corp., 862 F. Supp. 1502, 1509 (E.D. Va. 1994). In a U.S. Supreme Court case involving a former in-house lawyer suing his former employer under the False Claims Act, no one even raised the issue of whether that lawyer had violated his ethical obligations by bringing the qui tam suit. Vermont Agency of Natural Resources v. U.S. ex rel. Stevens, 529 U.S. 765 (2000).

If bar rules permit a lawyer to disclose client fraud, should that lawyer also be able to receive a financial award for that disclosure? At oral argument, the Second Circuit judges appeared to be concerned that the massive financial awards available under the False Claims Act might encourage lawyers to betray their clients, undermining clients' ability to trust their lawyers. Quest argues that the subsequent conflict-of-
interest rule prohibits a lawyer from serving as a relator in a case related to the work he did for a former cli-
ent. If the Second Circuit adopts that approach, former in-house lawyers will not be able to take advantage of
the financial incentives provided by the False Claims Act even when a confidentiality exception applies. But
that won't prevent lawyers from taking advantage of other whistleblower incentives.

The Dodd-Frank Act provides financial incentives for insiders who blow the whistle on securities fraud;
the SEC issued regulations explicitly permitting whistleblower awards to lawyers under some circumstances.
The SEC is receiving eight whistleblower tips per day, and in August issued its first whistleblower award,
granting the maximum allowable 30 percent recovery to a whistleblower. So no matter how the Second Cir-
cuit rules in this case, we can expect to see more lawyers seeking financial incentives for blowing the whistle
on their clients' fraud.

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FINANCIAL INCENTIVES FOR WHISTLEBLOWERS:
ISSUES FOR PLAINTIFFS’ AND DEFENDANTS’ LAWYERS

Partial Bibliography of Legal Sources

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Boston University Law School

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United States ex rel. Frazier v. IASIS Health Care Corp., 2012 WL 130332 (Jan. 10, 2012) (compliance officer who was a lawyer did not represent company as its attorney; sanctions awarded against relator’s counsel for inappropriate treatment of potentially privileged documents of the corporation)


X Corp. v. Doe, 816 F. Supp. 1086 (E.D. Va. 1993) (X Corp. II) (granting employer injunction against former in-house lawyer on basis that no exception to duty of confidentiality applied)

United States ex rel. Doe v. X Corp, 862 F .Supp. 1502 (E.D. Va. 1994) (X Corp. III) (disqualifying former in-house lawyer from serving as relator qui tam action because of state confidentiality rules)

Cafasso ex rel. United States v. General Dynamics C4 Systems, Inc., 2009 WL 1457036 (D.Az. 2009), aff’d, 637 F.3d 1047 (9th Cir. 2011) (enforcement of confidentiality agreements covering information provided by employee-whistleblower to government)


SECONDARY SOURCES:


Whistleblowers, Ethics, and the Federal False Claims Act

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2. FraudMail Alert No. 09-05-21, Civil False Claims Act: The False Claims Act is Amended for the First Time in More Than Twenty Years as the President Signs the Fraud Enforcement and Recovery Act of 2009

3. FraudMail Alert No. 10-03-24, Civil False Claims Act: Here They Go Again—Newly Enacted Comprehensive Health Care Reform Law Contains More FCA Amendments

4. FraudMail Alert No. 10-06-29, Civil False Claims Act: Here They Go Again, Round III: Financial Reform Bill Contains More FCA Amendments

5. Diagram of a Qui Tam Case

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8. FraudMail Alert No. 05-07-22, Internal Investigations: Fourth Circuit Provides Useful Guidance on Employee Interviews and the Attorney-Client Privilege

THE FEDERAL FALSE CLAIMS ACT
31 U.S.C. §§ 3729-3733

As amended by:


§ 3729. False claims

(a) LIABILITY FOR CERTAIN ACTS.—Any

(1) IN GENERAL.—Subject to paragraph (2), any person who—

(1A) knowingly presents, or causes to be presented, to an officer or employee of the United States Government or a member of the Armed Forces of the United States a false or fraudulent claim for payment or approval;

(2B) knowingly makes, uses, or causes to be made or used, a false record or statement material to get a false or fraudulent claim paid or approved by the Government;

(3C) conspires to defraud the Government by getting a false or fraudulent claim allowed or paid commit a violation of subparagraph (A), (B), (D), (E), (F), or (G);

(4D) has possession, custody, or control of property or money used, or to be used, by the Government and, intending to defraud the Government or willfully to conceal the property, knowingly delivers, or causes to be delivered, less property than the amount for which the person receives a certificate or receipt than all of that money or property;

(5E) is authorized to make or deliver a document certifying receipt of property used, or to be used, by the Government and, intending to
defraud the Government, makes or delivers the receipt without completely knowing that the information on the receipt is true;

(6E) knowingly buys, or receives as a pledge of an obligation or debt, public property from an officer or employee of the Government, or a member of the Armed Forces, who lawfully may not sell or pledge the property; or

(7G) knowingly makes, uses, or causes to be made or used, a false record or statement material to conceal, avoid, or decrease an obligation to pay or transmit money or property to the Government, or knowingly conceals or knowingly and improperly avoids or decreases an obligation to pay or transmit money or property to the Government, is liable to the United States Government for a civil penalty of not less than $5,000 and not more than $10,000, as adjusted by the Federal Civil Penalties Inflation Adjustment Act of 1990 (28 U.S.C. 2461 note; Public Law 104-410), plus 3 times the amount of damages which the Government sustains because of the act of that person, except that if

(2) REDUCED DAMAGES.—If the court finds that—

(A) the person committing the violation of this subsection furnished officials of the United States responsible for investigating false claims violations with all information known to such person about the violation within 30 days after the date on which the defendant first obtained the information;

(B) such person fully cooperated with any Government investigation of such violation; and

(C) at the time such person furnished the United States with the information about the violation, no criminal prosecution, civil action, or administrative action had commenced under this title with respect to such violation, and the person did not have actual knowledge of the existence of an investigation into such violation,

the court may assess not less than 2 times the amount of damages which the Government sustains because of the act of the person.

(3) COSTS OF CIVIL ACTIONS.—A person violating this subsection shall also be liable to the United States Government for the costs of a civil action brought to recover any such penalty or damages.

(b) KNOWING AND KNOWINGLY DEFINED.—For purposes of this section,
(1) the terms “knowing” and “knowingly” —

(A) mean that a person, with respect to information—

(j) has actual knowledge of the information;

(ii) acts in deliberate ignorance of the truth or falsity of the information; or

(iii) acts in reckless disregard of the truth or falsity of the information;

(B) require no proof of specific intent to defraud is required.

(c) CLAIM DEFINED.—For purposes of this section, the term “claim” includes—

(A) means any request or demand, whether under a contract or otherwise, for money or property which and whether or not the United States has title to the money or property, that—

(i) is presented to an officer, employee, or agent of the United States; or

(ii) is made to a contractor, grantee, or other recipient, if the money or property is to be spent or used on the Government’s behalf or to advance a Government program or interest, and if the United States Government —

(I) provides or has provided any portion of the money or property which is requested or demanded; or if the Government

(II) will reimburse such contractor, grantee, or other recipient for any portion of the money or property which is requested or demanded; and

(B) does not include requests or demands for money or property that the Government has paid to an individual as compensation for Federal employment or as an income subsidy with no restrictions on that individual’s use of the money or property;

(3) the term “obligation” means an established duty, whether or not fixed, arising from an express or implied contractual, grantor-grantee, or licensor-licensee relationship, from a fee-based or similar relationship, from statute or regulation, or from the retention of any overpayment; and
the term “material” means having a natural tendency to influence, or be capable of influencing, the payment or receipt of money or property.

EXEMPTION FROM DISCLOSURE.—Any information furnished pursuant to subparagraphs (A) through (C) of subsection (a)(2) shall be exempt from disclosure under section 552 of title 5.

EXCLUSION.—This section does not apply to claims, records, or statements made under the Internal Revenue Code of 1986.

§ 3730. Civil actions for false claims

(a) RESPONSIBILITIES OF THE ATTORNEY GENERAL.—The Attorney General diligently shall investigate a violation under section 3729. If the Attorney General finds that a person has violated or is violating section 3729, the Attorney General may bring a civil action under this section against the person.

(b) ACTIONS BY PRIVATE PERSONS.—

(1) A person may bring a civil action for a violation of section 3729 for the person and for the United States Government. The action shall be brought in the name of the Government. The action may be dismissed only if the court and the Attorney General give written consent to the dismissal and their reasons for consenting.

(2) A copy of the complaint and written disclosure of substantially all material evidence and information the person possesses shall be served on the Government pursuant to Rule 4(d)(4) of the Federal Rules of Civil Procedure. The complaint shall be filed in camera, shall remain under seal for at least 60 days, and shall not be served on the defendant until the court so orders. The Government may elect to intervene and proceed with the action within 60 days after it receives both the complaint and the material evidence and information.

(3) The Government may, for good cause shown, move the court for extensions of the time during which the complaint remains under seal under paragraph (2). Any such motions may be supported by affidavits or other submissions in camera. The defendant shall not be required to respond to any complaint filed under this section until 20 days after the complaint is unsealed and served upon the defendant pursuant to Rule 4 of the Federal Rules of Civil Procedure.

(4) Before the expiration of the 60-day period or any extensions obtained under paragraph (3), the Government shall—

(A) proceed with the action, in which case the action shall be conducted by the Government; or
(B) notify the court that it declines to take over the action, in which case the person bringing the action shall have the right to conduct the action.

(5) When a person brings an action under this subsection, no person other than the Government may intervene or bring a related action based on the facts underlying the pending action.

(c) RIGHTS OF THE PARTIES TO QUI TAM ACTIONS.—

(1) If the Government proceeds with the action, it shall have the primary responsibility for prosecuting the action, and shall not be bound by an act of the person bringing the action. Such person shall have the right to continue as a party to the action, subject to the limitations set forth in paragraph (2).

(2) (A) The Government may dismiss the action notwithstanding the objections of the person initiating the action if the person has been notified by the Government of the filing of the motion and the court has provided the person with an opportunity for a hearing on the motion.

(B) The Government may settle the action with the defendant notwithstanding the objections of the person initiating the action if the court determines, after a hearing, that the proposed settlement is fair, adequate, and reasonable under all the circumstances. Upon a showing of good cause, such hearing may be held in camera.

(C) Upon a showing by the Government that unrestricted participation during the course of the litigation by the person initiating the action would interfere with or unduly delay the Government’s prosecution of the case, or would be repetitious, irrelevant, or for purposes of harassment, the court may, in its discretion, impose limitations on the person’s participation, such as—

(i) limiting the number of witnesses the person may call;

(ii) limiting the length of the testimony of such witnesses;

(iii) limiting the person’s cross-examination of witnesses; or

(iv) otherwise limiting the participation by the person in the litigation.

(D) Upon a showing by the defendant that unrestricted participation during the course of the litigation by the person initiating the action would be for purposes of harassment or would cause the
defendant undue burden or unnecessary expense, the court may limit the participation by the person in the litigation.

(3) If the Government elects not to proceed with the action, the person who initiated the action shall have the right to conduct the action. If the Government so requests, it shall be served with copies of all pleadings filed in the action and shall be supplied with copies of all deposition transcripts (at the Government’s expense). When a person proceeds with the action, the court, without limiting the status and rights of the person initiating the action, may nevertheless permit the Government to intervene at a later date upon a showing of good cause.

(4) Whether or not the Government proceeds with the action, upon a showing by the Government that certain actions of discovery by the person initiating the action would interfere with the Government’s investigation or prosecution of a criminal or civil matter arising out of the same facts, the court may stay such discovery for a period of not more than 60 days. Such a showing shall be conducted in camera. The court may extend the 60-day period upon a further showing in camera that the Government has pursued the criminal or civil investigation or proceedings with reasonable diligence and any proposed discovery in the civil action will interfere with the ongoing criminal or civil investigation or proceedings.

(5) Notwithstanding subsection (b), the Government may elect to pursue its claim through any alternate remedy available to the Government, including any administrative proceeding to determine a civil money penalty. If any such alternate remedy is pursued in another proceeding, the person initiating the action shall have the same rights in such proceeding as such person would have had if the action had continued under this section. Any finding of fact or conclusion of law made in such other proceeding that has become final shall be conclusive on all parties to an action under this section. For purposes of the preceding sentence, a finding or conclusion is final if it has been finally determined on appeal to the appropriate court of the United States, if all time for filing such an appeal with respect to the finding or conclusion has expired, or if the finding or conclusion is not subject to judicial review.

(d) **Award to Qui Tam Plaintiff.**—

(1) If the Government proceeds with an action brought by a person under subsection (b), such person shall, subject to the second sentence of this paragraph, receive at least 15 percent but not more than 25 percent of the proceeds of the action or settlement of the claim, depending upon the extent to which the person substantially contributed to the prosecution of the action. Where the action is one which the court finds to be based primarily on disclosures of specific information (other than information provided by the person bringing the action) relating to allegations or
transactions in a criminal, civil, or administrative hearing, in a congressional, administrative, or Government [General] Accounting Office report, hearing, audit, or investigation, or from the news media, the court may award such sums as it considers appropriate, but in no case more than 10 percent of the proceeds, taking into account the significance of the information and the role of the person bringing the action in advancing the case to litigation. Any payment to a person under the first or second sentence of this paragraph shall be made from the proceeds. Any such person shall also receive an amount for reasonable expenses which the court finds to have been necessarily incurred, plus reasonable attorneys’ fees and costs. All such expenses, fees, and costs shall be awarded against the defendant.

(2) If the Government does not proceed with an action under this section, the person bringing the action or settling the claim shall receive an amount which the court decides is reasonable for collecting the civil penalty and damages. The amount shall be not less than 25 percent and not more than 30 percent of the proceeds of the action or settlement and shall be paid out of such proceeds. Such person shall also receive an amount for reasonable expenses which the court finds to have been necessarily incurred, plus reasonable attorneys’ fees and costs. All such expenses, fees, and costs shall be awarded against the defendant.

(3) Whether or not the Government proceeds with the action, if the court finds that the action was brought by a person who planned and initiated the violation of section 3729 upon which the action was brought, then the court may, to the extent the court considers appropriate, reduce the share of the proceeds of the action which the person would otherwise receive under paragraph (1) or (2) of this subsection, taking into account the role of that person in advancing the case to litigation and any relevant circumstances pertaining to the violation. If the person bringing the action is convicted of criminal conduct arising from his or her role in the violation of section 3729, that person shall be dismissed from the civil action and shall not receive any share of the proceeds of the action. Such dismissal shall not prejudice the right of the United States to continue the action, represented by the Department of Justice.

(4) If the Government does not proceed with the action and the person bringing the action conducts the action, the court may award to the defendant its reasonable attorneys’ fees and expenses if the defendant prevails in the action and the court finds that the claim of the person bringing the action was clearly frivolous, clearly vexatious, or brought primarily for purposes of harassment.

(e) **CERTAIN ACTIONS BARRED.**—
(1) No court shall have jurisdiction over an action brought by a former or present member of the armed forces under subsection (b) of this section against a member of the armed forces arising out of such person’s service in the armed forces.

(2) (A) No court shall have jurisdiction over an action brought under subsection (b) against a Member of Congress, a member of the judiciary, or a senior executive branch official if the action is based on evidence or information known to the Government when the action was brought.

(B) For purposes of this paragraph, “senior executive branch official” means any officer or employee listed in paragraphs (1) through (8) of section 101(f) of the Ethics in Government Act of 1978 (5 U.S.C. App.).

(3) In no event may a person bring an action under subsection (b) which is based upon allegations or transactions which are the subject of a civil suit or an administrative civil money penalty proceeding in which the Government is already a party.

(4)(A) No court shall have jurisdiction over an action or claim under this section based upon the public disclosure of, unless opposed by the Government, if substantially the same allegations or transactions were publicly disclosed--

(i) in a Federal criminal, civil, or administrative hearing, in which the Government or its agent is a party;

(ii) in a congressional, administrative, or Government Accountability Office, or other Federal report, hearing, audit, or investigation; or

(iii) from the news media,

unless the action is brought by the Attorney General or the person bringing the action is an original source of the information.

(B) For purposes of this paragraph, “original source” means an individual who has direct and independent knowledge of either (i) prior to a public disclosure under subsection (e)(4)(a), has voluntarily disclosed to the Government the information on which the allegations are based, or (2) who has knowledge that is independent of and materially adds to the publicly disclosed allegations or transactions, and who has voluntarily provided the information to the Government before filing an action under this section.
GOVERNMENT NOT LIABLE FOR CERTAIN EXPENSES.—The Government is not liable for expenses which a person incurs in bringing an action under this section.

FEES AND EXPENSES TO PREVAILING DEFENDANT.—In civil actions brought under this section by the United States, the provisions of section 2412(d) of title 28 shall apply.

Any employee who—Relief From Retaliatory Actions. —

1. IN GENERAL. — Any employee, contractor, or agent shall be entitled to all relief necessary to make that employee, contractor, or agent whole if that employee, contractor, or agent is discharged, demoted, suspended, threatened, harassed, or in any other manner discriminated against in the terms and conditions of employment by his or her employer because of lawful acts done by the employee on behalf of the employee or contractor, agent, or associated others in furtherance of an action under this section, including investigation for, initiation of, testimony for, or assistance in an action filed or to be filed under this section, shall be entitled to all relief necessary to make the employee whole. Such relief or other efforts to stop 1 or more violations of this subchapter.

2. RELIEF. —Relief under paragraph (1) shall include reinstatement with the same seniority status such that employee, contractor, or agent would have had but for the discrimination, 2 times the amount of back pay, interest on the back pay, and compensation for any special damages sustained as a result of the discrimination, including litigation costs and reasonable attorneys' fees. An employee may bring an action under this subsection may be brought in the appropriate district court of the United States for the relief provided in this subsection.

3. LIMITATION ON BRINGING CIVIL ACTION. —A civil action under this subsection may not be brought more than 3 years after the date when the retaliation occurred.

§ 3731. False claims procedure

(a) A subpoena [subpoena] requiring the attendance of a witness at a trial or hearing conducted under section 3730 of this title may be served at any place in the United States.

(b) A civil action under section 3730 may not be brought—

1. more than 6 years after the date on which the violation of section 3729 is committed, or

2. more than 3 years after the date when facts material to the right of action are known or reasonably should have been known by the official of the United States charged with responsibility to act in the circumstances, but
in no event more than 10 years after the date on which the violation is committed, whichever occurs last.

(c) If the Government elects to intervene and proceed with an action brought under 3730(b), the Government may file its own complaint or amend the complaint of a person who has brought an action under section 3730(b) to clarify or add detail to the claims in which the Government is intervening and to add any additional claims with respect to which the Government contends it is entitled to relief. For statute of limitations purposes, any such Government pleading shall relate back to the filing date of the complaint of the person who originally brought the action, to the extent that the claim of the Government arises out of the conduct, transactions, or occurrences set forth, or attempted to be set forth, in the prior complaint of that person.

(e)(d) In any action brought under section 3730, the United States shall be required to prove all essential elements of the cause of action, including damages, by a preponderance of the evidence.

Notwithstanding any other provision of law, the Federal Rules of Criminal Procedure, or the Federal Rules of Evidence, a final judgment rendered in favor of the United States in any criminal proceeding charging fraud or false statements, whether upon a verdict after trial or upon a plea of guilty or nolo contendere, shall estop the defendant from denying the essential elements of the offense in any action which involves the same transaction as in the criminal proceeding and which is brought under subsection (a) or (b) of section 3730.

§ 3732. False claims jurisdiction

(a) Actions Under Section 3730.—Any action under section 3730 may be brought in any judicial district in which the defendant or, in the case of multiple defendants, any one defendant can be found, resides, transacts business, or in which any act proscribed by section 3729 occurred. A summons as required by the Federal Rules of Civil Procedure shall be issued by the appropriate district court and served at any place within or outside the United States.

(b) Claims Under State Law.—The district courts shall have jurisdiction over any action brought under the laws of any State for the recovery of funds paid by a State or local government if the action arises from the same transaction or occurrence as an action brought under section 3730.

(c) Service on State of Local Authorities.—With respect to any State or local government that is named as a co-plaintiff with the United States in an action brought under subsection (b), a seal on the action ordered by the court under section 3730(b) shall not preclude the Government or the person bringing the action from serving the complaint, any other pleadings, or the written disclosure of substantially all material evidence and information possessed by the person bringing the action on the law enforcement authorities that are authorized under the law of that State or local government to investigate and prosecute such actions on behalf of such governments, except that such seal applies to the law enforcement authorities so served to the same extent as the seal applies to other parties in the action.

§ 3733. Civil investigative demands
(a) **IN GENERAL.**—

(1) **ISSUANCE AND SERVICE.**—Whenever the Attorney General, or a designee (for purposes of this section), has reason to believe that any person may be in possession, custody, or control of any documentary material or information relevant to a false claims law investigation, the Attorney General, or a designee, may, before commencing a civil proceeding under section 3730(a) or other false claims law, or making an election under section 3730(b), issue in writing and cause to be served upon such person, a civil investigative demand requiring such person—

(A) to produce such documentary material for inspection and copying,

(B) to answer in writing written interrogatories with respect to such documentary material or information,

(C) to give oral testimony concerning such documentary material or information, or

(D) to furnish any combination of such material, answers, or testimony.

The Attorney General may not delegate the authority to issue civil investigative demands under this subsection. Whenever a civil investigative demand is an express demand for any product of discovery, the Attorney General, the Deputy Attorney General, or an Assistant Attorney General shall cause to be served, in any manner authorized by this section, a copy of such demand upon the person from whom the discovery was obtained and shall notify the person to whom such demand is issued of the date on which such copy was served. Any information obtained by the Attorney General or a designee of the Attorney General under this section may be shared with any qui tam relator if the Attorney General or designee determine it is necessary as part of any false claims act investigation.

(2) **CONTENTS AND DEADLINES.**—

(A) Each civil investigative demand issued under paragraph (1) shall state the nature of the conduct constituting the alleged violation of a false claims law which is under investigation, and the applicable provision of law alleged to be violated.

(B) If such demand is for the production of documentary material, the demand shall—

(i) describe each class of documentary material to be produced with such definiteness and certainty as to permit such material to be fairly identified;
(ii) prescribe a return date for each such class which will provide a reasonable period of time within which the material so demanded may be assembled and made available for inspection and copying; and

(iii) identify the false claims law investigator to whom such material shall be made available.

(C) If such demand is for answers to written interrogatories, the demand shall—

(i) set forth with specificity the written interrogatories to be answered;

(ii) prescribe dates at which time answers to written interrogatories shall be submitted; and

(iii) identify the false claims law investigator to whom such answers shall be submitted.

(D) If such demand is for the giving of oral testimony, the demand shall—

(i) prescribe a date, time, and place at which oral testimony shall be commenced;

(ii) identify a false claims law investigator who shall conduct the examination and the custodian to whom the transcript of such examination shall be submitted;

(iii) specify that such attendance and testimony are necessary to the conduct of the investigation;

(iv) notify the person receiving the demand of the right to be accompanied by an attorney and any other representative; and

(v) describe the general purpose for which the demand is being issued and the general nature of the testimony, including the primary areas of inquiry, which will be taken pursuant to the demand.

(E) Any civil investigative demand issued under this section which is an express demand for any product of discovery shall not be returned or returnable until 20 days after a copy of such demand has been served upon the person from whom the discovery was obtained.
(F) The date prescribed for the commencement of oral testimony pursuant to a civil investigative demand issued under this section shall be a date which is not less than seven days after the date on which demand is received, unless the Attorney General or an Assistant Attorney General designated by the Attorney General determines that exceptional circumstances are present which warrant the commencement of such testimony within a lesser period of time.

(G) The Attorney General shall not authorize the issuance under this section of more than one civil investigative demand for oral testimony by the same person unless the person requests otherwise or unless the Attorney General, after investigation, notifies that person in writing that an additional demand for oral testimony is necessary. The Attorney General may not, notwithstanding section 510 of title 28, authorize the performance, by any other officer, employee, or agency, of any function vested in the Attorney General under this subparagraph.

(b) PROTECTED MATERIAL OR INFORMATION.—

(1) IN GENERAL.—A civil investigative demand issued under subsection (a) may not require the production of any documentary material, the submission of any answers to written interrogatories, or the giving of any oral testimony if such material, answers, or testimony would be protected from disclosure under—

(A) the standards applicable to subpoenas or subpoenas duces tecum issued by a court of the United States to aid in a grand jury investigation; or

(B) the standards applicable to discovery requests under the Federal Rules of Civil Procedure, to the extent that the application of such standards to any such demand is appropriate and consistent with the provisions and purposes of this section.

(2) EFFECT ON OTHER ORDERS, RULES, AND LAWS.—Any such demand which is an express demand for any product of discovery supersedes any inconsistent order, rule, or provision of law (other than this section) preventing or restraining disclosure of such product of discovery to any person. Disclosure of any product of discovery pursuant to any such express demand does not constitute a waiver of any right or privilege which the person making such disclosure may be entitled to invoke to resist discovery of trial preparation materials.

(c) SERVICE; JURISDICTION.—
(1) **By Whom Served.**—Any civil investigative demand issued under subsection (a) may be served by a false claims law investigator, or by a United States marshal or a deputy marshal, at any place within the territorial jurisdiction of any court of the United States.

(2) **Service in Foreign Countries.**—Any such demand or any petition filed under subsection (j) may be served upon any person who is not found within the territorial jurisdiction of any court of the United States in such manner as the Federal Rules of Civil Procedure prescribe for service in a foreign country. To the extent that the courts of the United States can assert jurisdiction over any such person consistent with due process, the United States District Court for the District of Columbia shall have the same jurisdiction to take any action respecting compliance with this section by any such person that such court would have if such person were personally within the jurisdiction of such court.

(d) **Service Upon Legal Entities and Natural Persons.**—

(1) **Legal Entities.**—Service of any civil investigative demand issued under subsection (a) or of any petition filed under subsection (j) may be made upon a partnership, corporation, association, or other legal entity by—

   (A) delivering an executed copy of such demand or petition to any partner, executive officer, managing agent, or general agent of the partnership, corporation, association, or entity, or to any agent authorized by appointment or by law to receive service of process on behalf of such partnership, corporation, association, or entity;

   (B) delivering an executed copy of such demand or petition to the principal office or place of business of the partnership, corporation, association, or entity; or

   (C) depositing an executed copy of such demand or petition in the United States mails by registered or certified mail, with a return receipt requested, addressed to such partnership, corporation, association, or entity at its principal office or place of business.

(2) **Natural Persons.**—Service of any such demand or petition may be made upon any natural person by—

   (A) delivering an executed copy of such demand or petition to the person; or

   (B) depositing an executed copy of such demand or petition in the United States mails by registered or certified mail, with a return receipt requested, addressed to the person at the person’s residence or principal office or place of business.
(e) **Proof of Service.**—A verified return by the individual serving any civil investigative demand issued under subsection (a) or any petition filed under subsection (j) setting forth the manner of such service shall be proof of such service. In the case of service by registered or certified mail, such return shall be accompanied by the return post office receipt of delivery of such demand.

(f) **Documentary Material.**—

(1) **Sworn Certificates.**—The production of documentary material in response to a civil investigative demand served under this section shall be made under a sworn certificate, in such form as the demand designates, by—

(A) in the case of a natural person, the person to whom the demand is directed, or

(B) in the case of a person other than a natural person, a person having knowledge of the facts and circumstances relating to such production and authorized to act on behalf of such person.

The certificate shall state that all of the documentary material required by the demand and in the possession, custody, or control of the person to whom the demand is directed has been produced and made available to the false claims law investigator identified in the demand.

(2) **Production of Materials.**—Any person upon whom any civil investigative demand for the production of documentary material has been served under this section shall make such material available for inspection and copying to the false claims law investigator identified in such demand at the principal place of business of such person, or at such other place as the false claims law investigator and the person thereafter may agree and prescribe in writing, or as the court may direct under subsection (j)(1).

Such material shall be made so available on the return date specified in such demand, or on such later date as the false claims law investigator may prescribe in writing. Such person may, upon written agreement between the person and the false claims law investigator, substitute copies for originals of all or any part of such material.

(g) **Interrogatories.**—Each interrogatory in a civil investigative demand served under this section shall be answered separately and fully in writing under oath and shall be submitted under a sworn certificate, in such form as the demand designates, by—

(1) in the case of a natural person, the person to whom the demand is directed, or

(2) in the case of a person other than a natural person, the person or persons responsible for answering each interrogatory.
If any interrogatory is objected to, the reasons for the objection shall be stated in the certificate instead of an answer. The certificate shall state that all information required by the demand and in the possession, custody, control, or knowledge of the person to whom the demand is directed has been submitted. To the extent that any information is not furnished, the information shall be identified and reasons set forth with particularity regarding the reasons why the information was not furnished.

(h) ORAL EXAMINATIONS.—

(1) PROCEDURES.—The examination of any person pursuant to a civil investigative demand for oral testimony served under this section shall be taken before an officer authorized to administer oaths and affirmations by the laws of the United States or of the place where the examination is held. The officer before whom the testimony is to be taken shall put the witness on oath or affirmation and shall, personally or by someone acting under the direction of the officer and in the officer’s presence, record the testimony of the witness. The testimony shall be taken stenographically and shall be transcribed. When the testimony is fully transcribed, the officer before whom the testimony is taken shall promptly transmit a copy of the transcript of the testimony to the custodian. This subsection shall not preclude the taking of testimony by any means authorized by, and in a manner consistent with, the Federal Rules of Civil Procedure.

(2) PERSONS PRESENT.—The false claims law investigator conducting the examination shall exclude from the place where the examination is held all persons except the person giving the testimony, the attorney for and any other representative of the person giving the testimony, the attorney for the Government, any person who may be agreed upon by the attorney for the Government and the person giving the testimony, the officer before whom the testimony is to be taken, and any stenographer taking such testimony.

(3) WHERE TESTIMONY TAKEN.—The oral testimony of any person taken pursuant to a civil investigative demand served under this section shall be taken in the judicial district of the United States within which such person resides, is found, or transacts business, or in such other place as may be agreed upon by the false claims law investigator conducting the examination and such person.

(4) TRANSCRIPT OF TESTIMONY.—When the testimony is fully transcribed, the false claims law investigator or the officer before whom the testimony is taken shall afford the witness, who may be accompanied by counsel, a reasonable opportunity to examine and read the transcript, unless such examination and reading are waived by the witness. Any changes in form or substance which the witness desires to make shall be entered and identified upon the transcript by the officer or the false claims law investigator, with a statement of the reasons given by the witness for making such changes. The transcript shall then be signed by the witness,
unless the witness in writing waives the signing, is ill, cannot be found, or refues to sign. If the transcript is not signed by the witness within 30 days after being afforded a reasonable opportunity to examine it, the officer or the false claims law investigator shall sign it and state on the record the fact of the waiver, illness, absence of the witness, or the refusal to sign, together with the reasons, if any, given therefor.

(5) CERTIFICATION AND DELIVERY TO CUSTODIAN.—The officer before whom the testimony is taken shall certify on the transcript that the witness was sworn by the officer and that the transcript is a true record of the testimony given by the witness, and the officer or false claims law investigator shall promptly deliver the transcript, or send the transcript by registered or certified mail, to the custodian.

(6) FURNISHING OR INSPECTION OF TRANSCRIPT BY WITNESS.—Upon payment of reasonable charges therefor, the false claims law investigator shall furnish a copy of the transcript to the witness only, except that the Attorney General, the Deputy Attorney General, or an Assistant Attorney General may, for good cause, limit such witness to inspection of the official transcript of the witness’ testimony.

(7) CONDUCT OF ORAL TESTIMONY.—

(A) Any person compelled to appear for oral testimony under a civil investigative demand issued under subsection (a) may be accompanied, represented, and advised by counsel. Counsel may advise such person, in confidence, with respect to any question asked of such person. Such person or counsel may object on the record to any question, in whole or in part, and shall briefly state for the record the reason for the objection. An objection may be made, received, and entered upon the record when it is claimed that such person is entitled to refuse to answer the question on the grounds of any constitutional or other legal right or privilege, including the privilege against self-incrimination. Such person may not otherwise object to or refuse to answer any question, and may not directly or through counsel otherwise interrupt the oral examination. If such person refuses to answer any question, a petition may be filed in the district court of the United States under subsection (j)(1) for an order compelling such person to answer such question.

(B) If such person refuses to answer any question on the grounds of the privilege against self-incrimination, the testimony of such person may be compelled in accordance with the provisions of part V of title 18 [18 USCS §§ 6001 et seq.].
(8) **WITNESS FEES AND ALLOWANCES.**—Any person appearing for oral testimony under a civil investigative demand issued under subsection (a) shall be entitled to the same fees and allowances which are paid to witnesses in the district courts of the United States.

(i) **CUSTODIANS OF DOCUMENTS, ANSWERS, AND TRANSCRIPTS.**—

(1) **DESIGNATION.**—The Attorney General shall designate a false claims law investigator to serve as custodian of documentary material, answers to interrogatories, and transcripts of oral testimony received under this section, and shall designate such additional false claims law investigators as the Attorney General determines from time to time to be necessary to serve as deputies to the custodian.

(2) **RESPONSIBILITY FOR MATERIALS; DISCLOSURE.**—

(A) A false claims law investigator who receives any documentary material, answers to interrogatories, or transcripts of oral testimony under this section shall transmit them to the custodian. The custodian shall take physical possession of such material, answers, or transcripts and shall be responsible for the use made of them and for the return of documentary material under paragraph (4).

(B) The custodian may cause the preparation of such copies of such documentary material, answers to interrogatories, or transcripts of oral testimony as may be required for official use by any false claims law investigator, or other officer or employee of the Department of Justice, who is authorized for such use under regulations which the Attorney General shall issue. Such material, answers, and transcripts may be used by any such authorized false claims law investigator or other officer or employee in connection with the taking of oral testimony under this section.

(C) Except as otherwise provided in this subsection, no documentary material, answers to interrogatories, or transcripts of oral testimony, or copies thereof, while in the possession of the custodian, shall be available for examination by any individual other than a false claims law investigator or other officer or employee of the Department of Justice authorized under subparagraph (B). The prohibition in the preceding sentence on the availability of material, answers, or transcripts shall not apply if consent is given by the person who produced such material, answers, or transcripts, or, in the case of any product of discovery produced pursuant to an express demand for such material, consent is given by the person from whom the discovery was obtained. Nothing in this subparagraph is intended to prevent disclosure to the Congress, including any committee or subcommittee of the
Congress, or to any other agency of the United States for use by such agency in furtherance of its statutory responsibilities. Disclosure of information to any such other agency shall be allowed only upon application, made by the Attorney General to a United States district court, showing substantial need for the use of the information by such agency in furtherance of its statutory responsibilities.

(D) While in the possession of the custodian and under such reasonable terms and conditions as the Attorney General shall prescribe—

(i) documentary material and answers to interrogatories shall be available for examination by the person who produced such material or answers, or by a representative of that person authorized by that person to examine such material and answers; and

(ii) transcripts of oral testimony shall be available for examination by the person who produced such testimony, or by a representative of that person authorized by that person to examine such transcripts.

(3) USE OF MATERIAL, ANSWERS, OR TRANSCRIPTS IN OTHER PROCEEDINGS.—Whenever any attorney of the Department of Justice has been designated to appear before any court, grand jury, or Federal agency in any case or proceeding, the custodian of any documentary material, answers to interrogatories, or transcripts of oral testimony received under this section may deliver to such attorney such material, answers, or transcripts for official use in connection with any such case or proceeding as such attorney determines to be required. Upon the completion of any such case or proceeding, such attorney shall return to the custodian any such material, answers, or transcripts so delivered which have not passed into the control of such court, grand jury, or agency through introduction into the record of such case or proceeding.

(4) CONDITIONS FOR RETURN OF MATERIAL.—If any documentary material has been produced by any person in the course of any false claims law investigation pursuant to a civil investigative demand under this section, and—

(A) any case or proceeding before the court or grand jury arising out of such investigation, or any proceeding before any Federal agency involving such material, has been completed, or

(B) no case or proceeding in which such material may be used has been commenced within a reasonable time after completion of the
examination and analysis of all documentary material and other information assembled in the course of such investigation,

the custodian shall, upon written request of the person who produced such material, return to such person any such material (other than copies furnished to the false claims law investigator under subsection (f)(2) or made for the Department of Justice under paragraph (2)(B)) which has not passed into the control of any court, grand jury, or agency through introduction into the record of such case or proceeding.

(5) APPOINTMENT OF SUCCESSOR CUSTODIANS.—In the event of the death, disability, or separation from service in the Department of Justice of the custodian of any documentary material, answers to interrogatories, or transcripts of oral testimony produced pursuant to a civil investigative demand under this section, or in the event of the official relief of such custodian from responsibility for the custody and control of such material, answers, or transcripts, the Attorney General shall promptly—

(A) designate another false claims law investigator to serve as custodian of such material, answers, or transcripts, and

(B) transmit in writing to the person who produced such material, answers, or testimony notice of the identity and address of the successor so designated.

Any person who is designated to be a successor under this paragraph shall have, with regard to such material, answers, or transcripts, the same duties and responsibilities as were imposed by this section upon that person’s predecessor in office, except that the successor shall not be held responsible for any default or dereliction which occurred before that designation.

(j) JUDICIAL PROCEEDINGS.—

(1) PETITION FOR ENFORCEMENT.—Whenever any person fails to comply with any civil investigative demand issued under subsection (a), or whenever satisfactory copying or reproduction of any material requested in such demand cannot be done and such person refuses to surrender such material, the Attorney General may file, in the district court of the United States for any judicial district in which such person resides, is found, or transacts business, and serve upon such person a petition for an order of such court for the enforcement of the civil investigative demand.

(2) PETITION TO MODIFY OR SET ASIDE DEMAND.—

(A) Any person who has received a civil investigative demand issued under subsection (a) may file, in the district court of the United States for the judicial district within which such person resides, is
found, or transacts business, and serve upon the false claims law investigator identified in such demand a petition for an order of the court to modify or set aside such demand. In the case of a petition addressed to an express demand for any product of discovery, a petition to modify or set aside such demand may be brought only in the district court of the United States for the judicial district in which the proceeding in which such discovery was obtained is or was last pending. Any petition under this subparagraph must be filed—

(i) within 20 days after the date of service of the civil investigative demand, or at any time before the return date specified in the demand, whichever date is earlier, or

(ii) within such longer period as may be prescribed in writing by any false claims law investigator identified in the demand.

(B) The petition shall specify each ground upon which the petitioner relies in seeking relief under subparagraph (A), and may be based upon any failure of the demand to comply with the provisions of this section or upon any constitutional or other legal right or privilege of such person. During the pendency of the petition in the court, the court may stay, as it deems proper, the running of the time allowed for compliance with the demand, in whole or in part, except that the person filing the petition shall comply with any portions of the demand not sought to be modified or set aside.

(3) PETITION TO MODIFY OR SET ASIDE DEMAND FOR PRODUCT OF DISCOVERY.—

(A) In the case of any civil investigative demand issued under subsection (a) which is an express demand for any product of discovery, the person from whom such discovery was obtained may file, in the district court of the United States for the judicial district in which the proceeding in which such discovery was obtained is or was last pending, and serve upon any false claims law investigator identified in the demand and upon the recipient of the demand, a petition for an order of such court to modify or set aside those portions of the demand requiring production of any such product of discovery. Any petition under this subparagraph must be filed—

(i) within 20 days after the date of service of the civil investigative demand, or at any time before the return date specified in the demand, whichever date is earlier, or
(ii) within such longer period as may be prescribed in writing by any false claims law investigator identified in the demand.

(B) The petition shall specify each ground upon which the petitioner relies in seeking relief under subparagraph (A), and may be based upon any failure of the portions of the demand from which relief is sought to comply with the provisions of this section, or upon any constitutional or other legal right or privilege of the petitioner. During the pendency of the petition, the court may stay, as it deems proper, compliance with the demand and the running of the time allowed for compliance with the demand.

(4) PETITION TO REQUIRE PERFORMANCE BY CUSTODIAN OF DUTIES.—At any time during which any custodian is in custody or control of any documentary material or answers to interrogatories produced, or transcripts of oral testimony given, by any person in compliance with any civil investigative demand issued under subsection (a), such person, and in the case of an express demand for any product of discovery, the person from whom such discovery was obtained, may file, in the district court of the United States for the judicial district within which the office of such custodian is situated, and serve upon such custodian, a petition for an order of such court to require the performance by the custodian of any duty imposed upon the custodian by this section.

(5) JURISDICTION.—Whenever any petition is filed in any district court of the United States under this subsection, such court shall have jurisdiction to hear and determine the matter so presented, and to enter such order or orders as may be required to carry out the provisions of this section. Any final order so entered shall be subject to appeal under section 1291 of title 28. Any disobedience of any final order entered under this section by any court shall be punished as a contempt of the court.

(6) APPLICABILITY OF FEDERAL RULES OF CIVIL PROCEDURE.—The Federal Rules of Civil Procedure shall apply to any petition under this subsection, to the extent that such rules are not inconsistent with the provisions of this section.

(k) DISCLOSURE EXEMPTION.—Any documentary material, answers to written interrogatories, or oral testimony provided under any civil investigative demand issued under subsection (a) shall be exempt from disclosure under section 552 of title 5.

(l) DEFINITIONS.—For purposes of this section—

(1) the term “false claims law” means—

(A) this section and sections 3729 through 3732; and
(B) any Act of Congress enacted after the date of the enactment of this section [enacted Oct. 27, 1986] which prohibits, or makes available to the United States in any court of the United States any civil remedy with respect to, any false claim against, bribery of, or corruption of any officer or employee of the United States;

(2) the term “false claims law investigation” means any inquiry conducted by any false claims law investigator for the purpose of ascertaining whether any person is or has been engaged in any violation of a false claims law;

(3) the term “false claims law investigator” means any attorney or investigator employed by the Department of Justice who is charged with the duty of enforcing or carrying into effect any false claims law, or any officer or employee of the United States acting under the direction and supervision of such attorney or investigator in connection with a false claims law investigation;

(4) the term “person” means any natural person, partnership, corporation, association, or other legal entity, including any State or political subdivision of a State;

(5) the term “documentary material” includes the original or any copy of any book, record, report, memorandum, paper, communication, tabulation, chart, or other document, or data compilations stored in or accessible through computer or other information retrieval systems, together with instructions and all other materials necessary to use or interpret such data compilations, and any product of discovery;

(6) the term “custodian” means the custodian, or any deputy custodian, designated by the Attorney General under subsection (i)(1); and

(7) the term “product of discovery” includes—

(A) the original or duplicate of any deposition, interrogatory, document, thing, result of the inspection of land or other property, examination, or admission, which is obtained by any method of discovery in any judicial or administrative proceeding of an adversarial nature;

(B) any digest, analysis, selection, compilation, or derivation of any item listed in subparagraph (A); and

(C) any index or other manner of access to any item listed in subparagraph (A); and

(8) the term “official use” means any use that is consistent with the law, and the regulations and policies of the Department of Justice, including use in connection with internal Department of Justice memoranda and reports;
communications between the Department of Justice and a Federal, State, or local government agency, or a contractor of a Federal, State, or local government agency, undertaken in furtherance of a Department of Justice investigation or prosecution of a case; interviews of any qui tam relator or other witness; oral examinations; depositions; preparation for and response to civil discovery requests; introduction into the record of a case or proceeding; applications, motions, memoranda and briefs submitted to a court or other tribunal; and communications with Government investigators, auditors, consultants and experts, the counsel of other parties, arbitrators and mediators, concerning an investigation, case or proceeding.

* * *

S. 386 Section 4(f):

EFFECTIVE DATE AND APPLICATION.—The amendments made by this section shall take effect on the date of enactment of the Act and shall apply to conduct on or after the date of enactment, except that—

(1) subparagraph (B) of section 3729(a)(1) of title 31, United States Code, as added by subsection (a)(1), shall take effect as if enacted on June 7, 2008, and apply to all claims under the False Claims Act (31 U.S.C. 3729 et seq.) that are pending on or after that date; and

(2) section 3731(b) of title 31, as amended by subsection (b); section 3733, of title 31, as amended by subsection (c); and section 3732 of title 31, as amended by subsection (e); shall apply to cases pending on the date of enactment.
Appendix 2
CIVIL FALSE CLAIMS ACT: The False Claims Act is Amended for the First Time in More Than Twenty Years as the President Signs the Fraud Enforcement and Recovery Act of 2009

Last night, the Fraud Enforcement and Recovery Act of 2009 (“FERA”) was signed into law by the President, marking only the second time in the history of the civil False Claims Act (“FCA”) that all-embracing amendments have been made to this 1863 law. After its first large-scale revision in 1936, the FCA became the government’s most successful weapon in its fight against suspected fraud on the United States, but it also became a weapon that competitors, disappointed bidders, disgruntled employees, and antagonistic agencies could use to punish and destroy those who opposed them. Congress’s stated purpose in passing the FERA was to expand the FCA’s liability provisions to reach frauds by financial institutions and other recipients of TARP and economic stimulus funds, but those funds were already covered by the FCA. The real purpose of these amendments is to overturn many decisions—like the unanimous Supreme Court decision last year in Allison Engine Co. v. United States ex rel. Sanders—which set logical and reasonable limits on the scope of the FCA, a punitive statute that has the power to destroy any individual, institution, municipal entity, or company subject to its provisions.

The new amendments will adversely affect everyone—all government contractors and subcontractors, all healthcare providers, every public and private grantee and sub-grantee, and every other person, company, and entity that pays money to the government or receives Federal funds—by making it far easier to conduct FCA investigations and to win FCA recoveries. Quite simply, many logical defenses have been eliminated, and those who deal in any way with the Federal government are entering a whole new world in which FCA liability is much broader and easier to prove.

Prior FraudMail Alerts have commented on the FCA amendments in the FERA throughout the legislative process. See FraudMail Alert Nos. 09-05-19; 09-05-15; 09-05-13; 09-05-06; 09-04-30. Here is a comprehensive look at these FCA amendments. A red-line version of the changes that have now become final is available here. Attached is the final version of the FCA that is effective as of May 20, 2009.
Major FCA Amendments Expanding Liability

Under the FERA, the key liability sections of the FCA remain the provisions addressing false claims, false statements supporting false claims, conspiracy, and the reverse false claims and obligation provisions. These provisions have been renumbered as well as expanded to cover additional conduct. The new sections 3729(a)(1)(A), (B), (C), and (G) extend liability to any person who:

(A) knowingly presents, or causes to be presented, a false or fraudulent claim for payment or approval;

(B) knowingly makes, uses, or causes to be made or used, a false record or statement material to a false or fraudulent claim;

(C) conspires to commit a violation of subparagraph (A), (B), (D), (E), (F), or (G);

[... ] or

(G) knowingly makes, uses, or causes to be made or used, a false record or statement material to an obligation to pay or transmit money or property to the Government, or knowingly conceals or knowingly and improperly avoids or decreases an obligation to pay or transmit money or property to the Government.

Many of the key changes are in the definitions, found in section 3729(b).

Elimination of Allison Engine's Intent Requirement:  Under the Supreme Court's unanimous decision in Allison Engine Co. v. United States ex rel. Sanders, 128 S. Ct. 2123 (2008), FCA liability was limited to fraudulent statements that were designed "to get" false claims paid or approved "by the Government." See FraudMail Alert No. 08-06-09. See also John. T. Boese, Civil False Claims and Qui Tam Actions §2.06[G] (3d ed. 2006 & Supp. 2009-1). The Supreme Court's interpretation in Allison Engine no longer applies after the FERA because the new law removes both the "to get" language and the "by the Government" limitation in section 3729(a)(2)—as well as comparable language in sections 3729(a)(3) and (a)(7). Further, it attempts to make those changes in section 3729(a)(1)(B) effective as of June 7, 2008—the date Allison Engine was decided.

The Court in Allison Engine found that, without a clear link between a false claim and payment or approval by the government, the FCA would be "boundless" and become an "all-purpose antifraud statute." 128 S. Ct. at 2128, 2130. To replace this rational limitation, the FERA adds a new definition of "claim," and FCA liability will be limited only by requiring some sort of nexus to the government. The FCA now covers requests for funds to a contractor, grantee, or other recipient, if the money or property requested "is to be spent or used on the Government's behalf or to advance a Government program or interest." The legislation does not define the key terms "used on the Government's behalf" or "to advance a Government program or interest," and presumably courts will have to decide their meaning on a case by case basis. No one knows the scope. Are government funds invested in GM or AIG "advancing a Government program" so that a false
claim to those entities will violate the FCA and be enforced by qui tam relators? Recognizing that this new language is not very clear, Senator Kyle attempted to limit its scope:

[p]revious understanding, as well as commons sense, dictate that a particular transaction does not "advance a Government program or interest" unless it is predominantly federal in character—something that at least would require . . . that the claim ultimately results in a loss to the government . . . [rather than] any garden-variety dispute between a general contractor and a subcontractor simply because the general receives some federal money.


Materiality Requirement: In addition to the nexus to the government requirement, the FERA, at long last, specifically incorporates a materiality requirement in the False Claims Act (a position the government and relators fought, without success, for over 15 years), but it defines "material" as "having a natural tendency to influence, or be capable of influencing, the payment or receipt of money or property," which is the "weaker" materiality standard that has been applied in some FCA cases. See John T. Boese, Civil False Claims and Qui Tam Actions §2.04 (Aspen Publishers) (3d ed. & Supp. 2009-2). How much of a difference will this make? That depends entirely on how literally courts will read this provision. Almost every violation or mistake is arguably "capable of influencing" a payment decision by the government, but many courts in the past have read this test as strongly limiting the application of the FCA. For example, despite applying this "weaker" materiality standard, at least two courts have held that violations of "conditions of participation" in a Federal healthcare program do not result in FCA violations. See United States ex rel. Conner v. Salina Reg'l Health Ctr., 543 F.3d 1211 (10th Cir. 2008); United States ex rel. Landers v. Baptist Mem'l Health Care Corp., 525 F. Supp. 2d 972 (W.D. Tenn. 2007).

Conspiracy: Under the prior FCA, the conspiracy section was drafted to cover only a conspiracy "to get a false claim paid or approved." Courts had properly interpreted this language to limit the conspiracy section to apply only to violations of then-subsection 3729(a)(1), and not to violations of the reverse false claim provision. Moreover, the conspiracy section required that the government pay the false claim. The new conspiracy section, 31 U.S.C. § 3729(a)(1)(C), expands the conspiracy section to include a conspiracy to commit a violation of any other substantive section of the FCA. The amendment also eliminates the need for the false claim to be paid or approved, and assesses liability for conspiring to commit the violation. Importantly, the word "knowingly" still does not appear in the language of the new conspiracy section, so the argument remains that a common law liability, including specific intent, is still required to prove a conspiracy under the FCA.

Liability for Overpayments: The amended reverse false claims liability provision in section 3729(a)(1)(G) quoted above extends new liability to "knowingly and improperly avoid[ing] or decea[ing] an obligation to pay or transmit money or property to the Government." Under this provision, there is no need for a person to have taken an affirmative act—a false statement or record—in order to conceal, avoid, or decrease the obligation to the government. This new
provision is even more dangerous because an “obligation” is specifically defined to include within the scope of FCA liability the retention of an overpayment from the government. The term “improperly” is intended to limit this liability, and would presumably exclude overpayments such as those under Medicaid that undergo a reconciliation process. Practitioners will be required, almost immediately after passage, to begin to advise clients whether they have received “overpayments” and the potential liability that could result from retention of such overpayments. Moreover, even though this provision is not retroactive, an overpayment is an overpayment, whether it occurred before or after May 20, 2009. The government and relators are almost certain to argue that this provision applies to overpayments made before the date of the legislation.

Expanded Definition of “Obligation”: The definition of “obligation” that triggers reverse false claims liability is expanded to encompass “an established duty, whether or not fixed” that arises from a contractual, grantee, licensee, or fee-based relationship, from a statute or regulation, or from the retention of any overpayment. According to government statements, this is intended to overturn, among other cases, the Sixth Circuit’s decision 10 years ago in United States ex rel. American Textile Manufacturers Institute, Inc. v. The Limited, Inc., 190 F.3d 729 (6th Cir. 1999) (“ATMI”), which defined “obligation” to include only established obligations to pay money to the government. In addition to extending new liability to the retention of overpayments, this expanded definition seeks to extend liability to duties to pay fees that were not covered previously because they were not fixed in all particulars. Whether much of an expansion is actually achieved under this provision remains to be seen because even the DOJ concedes that the new language is not intended to extend FCA liability to penalties or fines. (The reader should note that the author represented many of the defendants in the ATMI case.)

Effective Date: Under the effective date provision in the FERA, the FCA liability amendments would apply prospectively, with one important exception. The amendment to section 3729(a)(2) takes effect on the date that Allison Engine was decided—June 7, 2008—making that amendment retroactive. The retroactivity of this amendment will raise a host of practical problems in pending cases, and is almost certain to be challenged as unconstitutional because conduct which the Supreme Court defined as outside the scope of FCA liability is, retroactively, now a violation. Were this a normal civil statute, such retroactivity would be allowable. But the Supreme Court has already defined the FCA as an “essentially punitive” statute. Vermont Agency of Natural Res. v. United States ex rel. Stevens, 529 U.S. 765 (2000). Whether a clearly punitive statute can be applied retroactively is a completely different question.

Additional FCA Amendments

In addition to amending the FCA’s liability provisions, the FERA includes four other amendments that make recoveries and investigations under the FCA easier. These amendments are as follows:

Retaliation: The prohibition against retaliation is expanded to include a “contractor, or agent,” in addition to an employee—without requiring prohibited retaliatory acts to be taken by an “employer.” Under this unusually broad definition, a retaliation action could be based on many different types of relationships that do not involve an employment contract, which could lead to unintended consequences.
Civil Investigative Demands: Under the FCA as passed in 1986, the Attorney General had to personally approve a CID, which can require deposition testimony under oath, clearly a power and a potentially abusive power. Under FERA, the Attorney General is now authorized to appoint a designee to approve a civil investigative demand, and the Attorney General or designee may share the information obtained with “any qui tam relator if the Attorney General or designee determine it is necessary as part of any false claims act investigation.” In addition, “official use” is broadly defined, allowing the Justice Department to use the information in communications with government personnel, consultants, and counsel for other parties in matters concerning an investigation, case, or proceeding. The expanded use and sharing of CID responses with any qui tam relator, consultant, and counsel is potentially harmful to businesses and individuals, and in recognition of this, one hopes it will be narrowly and carefully circumscribed by the Justice Department to curb abuses.

Relation Back: The government’s complaint in intervention or amendment to a relator’s complaint relates back to the date of the original complaint. Under this amendment, the government could delay its intervention in ways that could dramatically undermine a defendant’s ability to defend itself. See, e.g., United States v. Baylor Univ. Med. Ctr., 469 F.3d 263 (2d Cir. 2006); United States ex rel. Health Outcomes Techs. v. Hallmark Health Sys., Inc., 409 F. Supp. 2d 43 (D. Mass. 2006).

Service on State or Local Authorities: The seal provision would not prevent the government or relator from serving the written disclosure, a qui tam complaint, or other pleading on state and local law enforcement authorities that investigate the case.

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Appendix 3
CIVIL FALSE CLAIMS ACT: Here They Go Again – Newly Enacted Comprehensive Health Care Reform Law Contains More FCA Amendments

In May of last year, Congress enacted a dramatic revision to the substantive provisions of the civil False Claims Act, but left alone the key jurisdictional “public disclosure / original source” bar put in place by Congress in 1986 to avoid parasitic qui tam suits. See FraudMail Alert No. 09-05-21 (discussing FCA amendments in the Fraud Recovery and Enforcement Act of 2009 (“FERA”)). In the FCA amendments in FERA, Congress refused to weaken the public disclosure bar, but that restraint did not last a full year.

The Patient Protection and Affordable Care Act, signed into law by the President on March 23, 2010, directly amends the FCA’s public disclosure bar and original source exception to expand private enforcement of qui tam actions beyond these long-established boundaries. The FCA-related amendments are not limited to FCA actions against health care companies, but instead apply to all individuals and organizations covered by the FCA. The new law also contains confusing provisions that attempt to bootstrap FCA definitions such as “knowingly” and “obligation” to enforcement actions against participants in health care programs without amending the FCA. Similarly, it defines certain conditions of eligibility as “material” conditions of entitlement to receive payment, a designation that does not necessarily accord with FCA case law on conditions of eligibility. There is no substantive legislative history on these FCA-related provisions and amendments, which is unfortunate for those trying to understand and abide by them. As with past FCA amendments, these changes will trigger extensive litigation, and courts will be forced to grapple with how to apply them in the years to come.

A red-line version of the new public disclosure provision can be found here.

The FCA’s Public Disclosure Bar is Amended

The FCA’s public disclosure bar is amended in major ways. The new law provides:

(4)(A) The court shall dismiss an action or claim under this section, unless opposed by the Government, if substantially the same allegations or transactions as alleged in the action or claim were publicly disclosed—
(i) in a Federal criminal, civil, or administrative hearing in which the Government or its agent is a party;

(ii) in a congressional, Government Accountability Office, or other Federal report, hearing, audit, or investigation; or

(iii) from the news media, unless the action is brought by the Attorney General or the person bringing the action is an original source of the information.

(B) For purposes of this paragraph, “original source” means an individual who either (i) prior to a public disclosure under subsection (e)(4)(a), has voluntarily disclosed to the Government the information on which allegations or transactions in a claim are based, or (2) who has knowledge that is independent of and materially adds to the publicly disclosed allegations or transactions, and who has voluntarily provided the information to the Government before filing an action under this section.


The new public disclosure bar maintains the essential structure of the prior bar by requiring a court to dismiss a whistleblower’s *qui tam* suit if the allegations were “publicly disclosed,” unless the relator is an “original source” of the information underlying the allegations. However, the reach of the new public disclosure provision is limited by the following revisions:

- Dismissal is not required if the government opposes it;
- Only *federal* hearings in which the government ‘or its agent’ is a party are considered public disclosures of *qui tam* allegations;
- Only a *federal* report, hearing, audit or investigation qualifies as a public disclosure.

While the word “jurisdiction” has been removed, the use of the words “shall dismiss” means that the provision is similar to jurisdiction in that this issue should be resolved before the substantive case goes forward. Because the public disclosure bar is limited to federal hearings, however, fewer proceedings will be considered “public” and trigger the bar; fewer reports, audits, or investigations will trigger it for the same reason. Thus, although the question of whether a state report qualifies as a public disclosure is currently pending before the Supreme Court in *Graham County Soil & Water Conservation District v. United States ex rel. Wilson*, No. 08-304, that issue would be moot in future cases to which the amendment applies. See FraudMail Alert No. 09-11-30. Importantly, the “news media” prong of the public disclosure bar is unchanged.

The new “original source” amendments also expand the exception to the public disclosure bar by eliminating the requirement that a person must have “direct” knowledge of the information underlying the allegations. This revision, however, does not eliminate the need for some firsthand knowledge, which is the very essence of a true whistleblower; otherwise, it would allow anyone who acquired information secondhand from public sources to bring a *qui tam* suit and share in any recovery. With the new changes, a person with such “independent” knowledge must “materially add” to the publicly disclosed allegations to qualify as an original source. It is not clear exactly what is intended by the language “materially add,” which is not defined in the law. There does not
appear to be any intent by Congress, however, to overturn the result in *Rockwell International Corp. v. United States ex rel. Stone*, 549 U.S. 457 (2007), where the Supreme Court required the relator’s knowledge to encompass the allegations of fraud that were actually tried in the case, rather than simply to predict the ineffectiveness of a planned method of waste disposal that was never used. See FraudMail Alert Nos. 07-04-11 and 07-03-27. More importantly, the dual purposes of the bar—encouraging whistleblowers to alert the government to fraud while preventing parasitic suits—which date back to the statute’s origins, appear to remain intact after this revision.

Nothing in the new amendments to the FCA appears to express congressional intent for any of these changes to apply retroactively. Under the teaching of *Hughes Aircraft Co. v. United States ex rel. Schumer*, 520 U.S. 939 (1997), that should mean that this new language would apply only to conduct occurring after March 23, 2010.

**Attempts to Apply FCA Liability and Definitions in New Health Care Contexts**

The other FCA “amendments” in the new health law are truly bizarre. The new law attempts to apply several of the FCA’s definitions to various health care transactions without amending the FCA’s liability provisions to cover these transactions. For example, a program integrity provision governing enforcement of retained overpayments states that an overpayment retained beyond the deadline for reporting and returning it is an “obligation” as defined in the FCA. See H.R. 3590, § 6402(a). The provision also states that “knowingly” is defined as it is defined for purposes of the FCA, but the term “knowingly” does not appear in the provision on overpayments. Rather, the new provision requires reporting or return of an overpayment within 60 days after it was “identified”—a term that the provision does not define.

Despite this attempt to attach FCA liability using the definitions (or lack thereof) provided in the new enforcement provisions, the FCA itself governs liability based on “knowingly” avoiding or decreasing an “obligation.” Under the FCA, “obligation” is defined to include retention of an overpayment, but the FCA’s reverse false claims liability is limited to “knowingly and improperly” avoiding or decreasing an obligation, which requires the element of bad faith rather than the “identification”—however that term is defined—of an overpayment. See John T. Boese, Civil False Claims and Qui Tam Actions § 2.01[L] (Aspen Law & Business) (3d ed. 2006 & Supp. 2010-1).

The amendments provide a sense of the Congress relating to false claims and “payments made by, through, or in connection with an Exchange.” For example, the law’s tax credit and cost-sharing reduction provisions, which apply to health insurance exchanges, contain the statement that any payment in connection with an exchange that includes federal funds is subject to the FCA. The amendments contain language that would raise the FCA damages for such false claims to exchanges to an amount “not less than 3 times and not more than 6 times the amount of damages which the Government sustains,” but in another amendment, that language is declared null and void. See H.R. 3590, § 10104(j)(1).

Finally, the amendments provide:

Compliance with the requirements of this Act concerning eligibility for a health insurance issuer to participate in the Exchange shall be a material condition of an
issuer’s entitlement to receive payments, including payments of premium tax credits and cost-sharing reductions, through the Exchange.

H.R. 3590, § 1313(a)(6). This provision equates requirements for eligibility—whether important, unimportant, general, or specific—with a material condition of entitlement to payment. But, under the FCA, conditions of eligibility are not necessarily conditions of payment without a strong showing of materiality. See, e.g., United States ex rel. Conner v. Salina Reg’l Health Ctr., 543 F.3d 1211 (10th Cir. 2008); United States ex rel. Landers v. Baptist Mem’l Health Care Corp., 525 F. Supp. 2d 972 (W.D. Tenn. 2007). While these conditions of eligibility—many of which are yet to be established—may indeed be material under the FCA, a general statement that includes all of them does not necessarily suffice under the FCA. See John T. Boese, Civil False Claims and Qui Tam Actions, § 2.04 & n. 637 (citing cases). Also, the new law does not explain whether or how improper tax credit claims could be subject to FCA liability in light of the FCA’s tax exception. See 31 U.S.C. § 3729(d).

* * *

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CIVIL FALSE CLAIMS ACT: Here They Go Again, Round III: Financial Reform Bill Contains More FCA Amendments

It seems that Congress cannot let any opportunity to amend the False Claims Act go to waste, and this month’s legislative frenzy brings with it yet another amendment to the FCA, the third amendment in a little over a year. The House-Senate Conference Committee for the financial reform bill has approved two amendments to the so-called “whistleblower protection” provision of the FCA, 31 U.S.C. § 3730(h). See H.R. 4173, 111th Cong. (2010). After Congress completely botched the amendment of this section in the FERA amendments in 2009, see FraudMail Alert No. 09-05-21, the Committee has approved amendments that will (1) once again revise the definition of “protected conduct,” and (2) provide, for the first time, a three-year statute of limitations for actions brought under Section 3730(h), resolving the issue the Supreme Court addressed in Graham County Soil & Water Conservation District v. United States ex rel. Wilson, 545 U.S. 409 (2005) (“Graham County I”). See FraudMail Alert No. 05-06-20. A redline comparison of the Committee’s and FERA’s retaliation amendments is attached.

Because the Committee’s amendments redefining “protected conduct” would remove defenses to retaliation suits, if enacted, these amendments should only apply prospectively to conduct occurring after their date of enactment. Even applying the amendments prospectively introduces new terms and issues for interpretation that will add to the thicket of alternatives already facing litigants and judges in this fast-changing area of the law.

“Protected Conduct” Amendments

Prior to the FCA amendments in the Fraud Enforcement and Recovery Act of 2009 (“FERA”), a retaliation claim under Section 3730(h) required three basic elements: (1) the employee engaged in “protected conduct,” defined as lawful acts in furtherance of an FCA action, (2) the employer knew about the protected conduct, and (3) the employer retaliated against the employee because of the protected conduct. See John T. Boese, Civil False Claims and Qui Tam Actions §§4.11[B] (Aspen Publishers, Wolters Kluwer Law & Business) (3d ed. 2006 & Supp. 2010-1). FERA expanded the group of protected persons to “any employee, contractor, or agent,” and it removed the reference to discrimination by an “employer.” The reason for these changes was to eliminate the requirement that an employee-employer relationship was necessary for a retaliation violation—a requirement that excluded independent contractors from bringing retaliation actions. See id. at §§4.11[B][2][b].
FERA also changed the conduct required for protection—from lawful acts "in furtherance of an action under this section," to "other efforts to stop 1 or more violations." Thus, to prove retaliation under FERA, rather than investigating the fraud in order to file a qui tam suit, the person must actually try to stop the fraud itself. This narrowed, rather than enlarged, the retaliation cause of action. The Committee's amendment restores the original scope of protected conduct so that lawful acts in furtherance of a qui tam suit as well as "other efforts to stop 1 or more violations" are both covered. However, the Committee amendment also broadens the definition of conduct beyond the new boundaries established under FERA by expanding the group of actors who may engage in the conduct to include "associated others." This ambiguous terminology undoubtedly will be used to support whistleblower retaliation claims based on the conduct of persons and businesses that are not in any relationship with employers, and therefore would apply in circumstances well beyond FERA's independent contractor rationale. The only other requirement for this protection is that the conduct of the associated others must be "lawful."

In any event, the new relationships and requirements in FERA and the latest amendments are subject to conflicting interpretations. Defining protected conduct of an "employee," "contractor," "agent," and "associated others," as well as determining what qualifies as discrimination "in the terms and conditions of employment" by non-employers, will surely be subject to debate and litigation. Because these amendments are substantive—they seemingly would enlarge liability and remove defenses—any dispute over which version of Section 3730(h) applies should be resolved under the principles that govern retroactive application of amendments to conduct occurring before their enactment, rather than by simply applying the newest version of the law. See Graham County Soil & Water Conservation Dist. v. United States ex rel. Wilson, 130 S. Ct. 1396, 1400 n.1 (2010); Hughes Aircraft Co. v. United States ex rel. Schumer, 520 U.S. 939, 948 (1997).

**Statute of Limitations Amendment**

For the first time, the Committee has added a statute of limitations for retaliation in Section 3730(h), which requires these claims to be brought no more than three years from the date when the retaliation occurred. The lack of any statute of limitations for retaliation had prompted the Supreme Court to determine what limitation should be applied in *Graham County I*. The relator and the United States took the position in *Graham County I* that applying the FCA's six-year limitation on qui tam actions would serve the purposes of uniformity and certainty, but the Court rejected their interpretation as unsupported by the statute itself and because it would lead to absurd results. Indeed, the Court found that substantive FCA violations and retaliation were separate causes of action, that a substantive violation of the FCA was not required for a violation of Section 3730(h), and that the limit for retaliation should begin to run when the cause of action for that violation accrued rather than when a substantive FCA violation occurred. The Court established a default rule under which state statutes of limitations for analogous state causes of action are applied to FCA retaliation actions.

The Committee's three-year statute of limitations amendment finally fills the void that the Supreme Court's default rule addressed in *Graham County I*. While a three-year limitation is longer than many analogous state statutes of limitations, uniformity will eventually be achieved when this amendment takes effect.
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"Diagram of a Qui Tam Case"
*Civil False Claims and Qui Tam Actions, Third Edition*
by John T. Boese
Appendix 6

The “Players” in an Internal Investigation

Corporation/Institution
- Board of Directors
- Audit/Compliance Committee
- Special Committee

Corporate employees (officers)
- Individual employee counsel
- “Witness” counsel
- Joint defense agreements

In-house counsel
- General Counsel
- Division/unit counsel
- Internal audit
- Compliance officer

Outside counsel for the corporation
- Corporate counsel
- Board counsel
- “Special committee of board” counsel

“The Government”
- Government prosecutors/criminal
- Government prosecutors/civil
- Agency and agency counsel/administrative/civil
- Investigating agency
  o Office of Inspector General
  o FBI
- State AG Offices
  o Securities
  o Healthcare

Third party litigation attorneys adverse to company
- Securities class action counsel
- Tort claimant counsel
- Whistleblowers/qui tam lawyers
- Wrongful discharge lawyers for former employees
- Etc.
Appendix 7

The “Steps” of an Internal Investigation

1. Triggering event
   A. Internal
      - hotline call
      - employee debriefing
      - audit report
      - etc.
   B. External
      - grand jury subpoena
      - IG subpoena
      - letter/call from AUSA
      - newspaper article
      - threat from lawyers/lawsuit
      - etc.

2. Freeze the documents (mostly electronic)
   - 18 USC §1819

3. Decide on in-house vs. outside counsel to conduct the investigation
   - Long-time attorney/client relationship between in-house counsel and employees
   - Outside counsel usually has no such relationship

4. Gathering and reviewing documents
   - For internal investigation
   - For government
   - Waiver demands

5. Interviewing the employees
   - “The Dance”

6. Referring employees to outside counsel
   - Payment
   - KPMG decision

7. Joint defense agreements
8. Negotiations with government
   - Criminal
   - Civil
   - Administrative
   - Waiver demands
INTERNAL INVESTIGATIONS: Fourth Circuit Provides Useful Guidance on Employee Interviews and the Attorney-Client Privilege

The U.S. Court of Appeals for the Fourth Circuit issued a recent decision that addresses critical instructions given to employees during investigations conducted by inside or outside counsel. *See In re Grand Jury Subpoena, 2005 WL 1663786* (4th Cir. July 18, 2005). The court considered whether employees of AOL Time Warner could prevent the company from waiving the attorney-client privilege when responding to a grand jury subpoena for interview memos generated during the internal investigation. Three employees claimed they were represented personally by the investigating attorneys during interviews conducted between March and June 2001. The employees did not consent to the waiver, but their motion to quash was denied by the district court in a decision affirmed this week by the court of appeals. The Fourth Circuit panel held that all of the “essential touchstones for the formation of an attorney-client relationship between the investigating attorneys and the appellants were missing at the time of the interviews.” Id. at *3. However, the court also cautioned that language used by outside counsel in its instructions to company employees created “a potential legal and ethical mine field.” Id. at *5.

Instructions Given During Employee Interviews

The potentially troublesome language referred to by the court was a statement by outside counsel that although they represented AOL, they “could” represent the individuals too, “as long as no conflict appear[ed].” Id. at *1. The employees also received the following standard instruction from the outside lawyers:

We represent the company. These conversations are privileged, but the privilege belongs to the company and the company decides whether to waive it. If there is a conflict, the attorney-client privilege belongs to the company.

Id.

*continued on page 2*
When a grand jury issued a subpoena for documents relating to the interviews, AOL agreed to waive the attorney-client privilege and produce the documents. The three employees moved to quash, asserting that they each had an individual attorney-client relationship with the investigating attorneys, and that they refused to waive the privilege. Id. at *2.

The Common Interest Agreement With Wakeford

Further complicating matters was the fact that AOL's attorneys entered into a common interest agreement with one of the employees (Wakeford) roughly six months after the disputed interviews occurred. The common interest agreement related to an SEC investigation into an AOL matter. (Unlike the other two employees who moved to quash the grand jury subpoena, Wakeford was subsequently indicted, and therefore identified by the court in this decision.)

No Attorney-Client Relationship With the Employees

The district court denied the motion to quash as to all of the employees, and a unanimous panel of the Fourth Circuit affirmed, relying in part on the well-established principle that it takes more than an individual’s subjective belief to establish an attorney-client relationship. Id. at *4. Both courts ruled that the statement that the investigating attorneys could represent the individual in the absence of a conflict was not enough “to establish the reasonable understanding that they were representing” the employees. Id. at *3 (emphasis in original).

The Fourth Circuit ruled that the “essential touchstones” of an attorney-client relationship were missing under these facts, as demonstrated by the following:

- there was “no evidence of an objectively reasonable, mutual understanding that the appellants were seeking legal advice from the investigating attorneys or that the investigating attorneys were rendering personal legal advice;”

- the investigating attorneys clearly disclosed that:
  - they represented AOL;
  - the attorney-client privilege was solely AOL’s; and
  - the right to waive that privilege belonged solely to AOL;

- there was no evidence that the individual employees were told that the investigating attorneys represented them, and

- there was no evidence that any of the individuals asked for personal legal advice from the investigating attorneys, or that the investigating attorneys gave such advice to the individuals. Id. at *4.

Finally, Wakeford's common interest agreement did not preclude AOL’s waiver, the court held, because the agreement was not entered into until after the relevant interviews had already occurred.
The Dangers of the “Watered-Down Upjohn Warnings”

Nevertheless, the court of appeals expressed significant misgivings over the propriety of the “watered down Upjohn warnings” given to the appellants by the investigating attorneys (An “Upjohn warning” is one in which a company employee is advised that counsel represents the company, rather than the employee. This refers to a decision, Upjohn v. United States, 449 U.S. 383 (1981), in which the Supreme Court set forth the requirements that must be satisfied in order to protect communications with corporate employees under the attorney-client privilege.)

The Fourth Circuit considered the statement that the attorneys could represent the employees “if no conflict appeared[]” to be “a potential legal and ethical minefield.” The court noted that the attorneys would have been required to withdraw from all representation and maintain all confidences if a conflict arose after the investigating attorneys entered into an attorney-client relationship with both the employees and the company. These troubling issues were averted, the court held, only because no such relationship existed with the employees under these facts. id.

Best Practices for Employee Interviews During Internal Investigations:

Under Upjohn and the Fourth Circuit’s recent decision, the following practices are well established as best practices when conducting internal investigations:

- Company counsel (inside or outside) should warn (and document that they have warned) company employees at the very beginning of an internal investigation interview that:
  - counsel represents only the company, and not the employee personally;
  - the attorney-client privilege under which the interview is conducted belongs solely to the company and
  - only the company will decide whether any facts learned in the interview will be shared with any third party, including government officials.

It will be the decision of counsel regarding how best to establish these critical warnings. While some might recommend that these warnings be delivered in writing, and perhaps signed by the employees, others simply recommend that a standard script be given, without exception to each employee to be interviewed, with a mandatory requirement that the employee state that (s)he understands these conditions. How this is handled may vary by company, employee and investigation.
If you would like to receive a copy of the decisions discussed above, or if you have questions regarding this area, please contact us at fraudmail@frlnj.com or (202) 659-7220.

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Internal Investigations After Sarbanes-Oxley:
Best Practices in Avoiding Obstruction of Justice

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Internal Investigations After Sarbanes-Oxley: Best Practices in Avoiding Obstruction of Justice

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Fried, Frank, Harris, Shriver & Jacobson

I. Introduction

Many in-house and outside counsel have developed a standard method for conducting internal investigations. The recent spate of allegations and charges against major companies, and the enactment of the Sarbanes-Oxley Act of 2002 (the "Act")\(^1\), require corporate counsel to take another look at many assumptions and practices that, until recently, were not necessarily considered inappropriate. A careful and timely review of a company’s policy and practice in the key portions of any internal investigation -- document retention, gathering, and destruction; witness interviews and debriefings; and reporting the investigation’s results to the government -- can help in-house counsel avoid obstruction of justice charges like those that have brought so many difficulties upon other companies.

Moreover, the Department of Justice recently issued a revision to its policy on "Bringing Criminal Charges Against Corporations." That policy, originally issued by former Deputy Attorney General Eric Holder was updated in a memorandum circulated on January 20, 2003 by Deputy Attorney General Larry Thompson. (The Thompson Memorandum is attached as Tab 1.) In that memorandum, the Justice Department specifically notes that:

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The main focus of the revisions is increased emphasis on and scrutiny of the authenticity of a corporation's cooperation. Too often business organizations, while purporting to cooperate with a Department investigation, in fact take steps to impede the quick and effective exposure of the complete scope of wrongdoing under investigation. The revisions make clear that such conduct should weigh in favor of a corporate prosecution. The revisions also address the efficacy of the corporate governance mechanisms in place within a corporation, to ensure that these measures are truly effective rather than mere paper programs.2

A number of factors are listed in the Thompson Memorandum as indicia that a corporation is engaging in conduct that "impedes an investigation" despite assertions of cooperation. Those factors include what the Justice Department characterizes as "overly broad assertions of corporate representation of employees or former employees; inappropriate directions to employees or their counsel, such as directions not to cooperate openly and fully with the investigation including, for example, the direction to decline to be interviewed; making presentations or submissions that contain misleading assertions or omissions; incomplete or delayed production of records; and failure to promptly disclose illegal conduct known to the corporation."3

One final point bears emphasis. This is not a law journal article and does not express “the law” in every case. These are suggested “best practices” to be used as a guide. Each case is different, and each case requires a studied and deliberate consideration of the proper practices and procedures to be used.

II. Avoiding Obstruction of Justice in the Context of an Internal Investigation

There are four critical areas of an internal investigation that can give rise to obstruction of justice or witness tampering allegations against corporate counsel:

A. Gathering and reviewing responsive documents;

B. Communicating with employees and other potential witnesses;

2 Thompson Memorandum, Tab 1, at 1 (emphasis added).
3 Id. at insert page number.
C. Interviewing, preparing and debriefing witnesses; and

D. Reporting to the government.

Each of these areas is discussed in greater detail below.

A. **Gathering, Retaining, and Destroying Documents**

   The substance of a document retention and destruction policy is industry-specific, governed by a variety of regulatory, statutory and contractual standards. Such policies require careful monitoring on an ongoing basis, and may need to be revised in light of new mandates under the Sarbanes-Oxley Act.

   Although it is usually not necessary to suspend a document destruction policy completely during the course of an internal investigation, all employees should be notified, immediately and in writing, that no potentially relevant documents should be destroyed until after a custodian determines whether or not they are relevant. The problem with any destruction is an obvious one -- once a document is destroyed, there is no way to prove what it contained. Therefore, any destruction of a marginally relevant document should be avoided.

   There are a number of steps that can be followed to avoid the risk of being charged with obstructing justice.

   1. **Actions Prior to Receipt of a Subpoena or Document Request**

      Usually, a company is aware of a government investigation before any subpoena or formal request had been issued. During this time, in-house counsel must be extremely careful to avoid the potential charge that documents are being intentionally destroyed to impede a future investigation. This is essential now that the Sarbanes-Oxley Act has created new criminal provisions that impose heavy fines and significant prison terms on any person who, with criminal intent, performs acts including the knowing alteration, destruction, and falsification of documents relating to certain pending and contemplated investigations or other official
proceedings.\textsuperscript{4} Other document retention provisions in the Act apply specifically to accounting work papers.

- Specifically, newly-enacted provisions to be codified at 18 U.S.C. § 1519, state that:

$$\text{Whoever knowingly alters, destroys, mutilates, conceals, covers up, falsifies, or makes a false entry in any record, document or tangible object with the intent to impede, obstruct, or influence the investigation or proper administration of any matter within the jurisdiction of any department or agency of the United States or any case filed under title 11, or in relation to or contemplation of any such matter or case, shall be fined under this title, imprisoned not more than 20 years, or both.}$$

- Amendments to 18 U.S.C. § 1512 provide for the insertion of a new subsection (c), which states that:

$$(c) \text{ Whoever corruptly -}$$

$$(1) \text{ alters, destroys, mutilates, or conceals a record, document, or other object, or attempts to do so, with the intent to impair the object's integrity or availability for use in an official proceeding; or}$$

$$\text{(2) otherwise obstructs, influences, or impedes any official proceeding, or attempts to do so,}$$

$$\text{shall be fined under this title or imprisoned not more than 20 years, or both.}$$

President Bush's July 30, 2002 statement regarding the signing of the Sarbanes-Oxley Act notes that:

$$\text{To ensure that no infringement on the constitutional right to petition the Government for redress of grievances occurs in the enforcement of section 1512(c) of title 18 of the U.S. Code, enacted by section 1102 of the Act, which among other things prohibits corruptly influencing any official proceeding, the executive branch shall construe the term "corruptly" in section 1512(c)(2) as requiring proof of a criminal state of mind on the part of the defendant.}\textsuperscript{5}$$

- Sections 103(a)(2) and 802 of the Sarbanes-Oxley Act contain provisions regarding audit record retention. These provisions contain inconsistent time


periods for retaining audit and review workpapers, with Section 103(a)(2)(A)(i) requiring their retention for not less than seven years. Section 802 of the Act, which amends title 18 to add new Section 1520, requires certain accountants to maintain all audit or review workpapers for five years from the end of the fiscal period in which the audit or review was conducted. The SEC issued regulations regarding the retention of these records in early 2003.6 The knowing and wilfull violation of 18 U.S.C. § 1520 is subject to criminal fines and imprisonment of up to ten years.

Once a company has begun an internal investigation or, under the yet-to-be-tested language of Sarbanes-Oxley, certain official federal proceedings (including bankruptcy) are contemplated, counsel must make every effort to be certain that relevant documents are not destroyed. Employees and officers should be advised to retain their documents in a safe and secure location, preferably as kept in the normal course of business, until they can be gathered and reviewed as part of the internal investigation.

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6 For analysis of the new regulations, see the Fried, Frank web page, at http://www.ffhsj.com/cmemos/030205_retention_records.htm.
2. **Actions After Receipt of a Government Subpoena or Request**

   a. **Determine the Scope of the Subpoena**

   Relying on legal rights does not constitute obstruction of justice, and a company or individual may reject informal document requests and insist on a formal subpoena. If a subpoena is served, compliance with a formal subpoena is mandatory, unless the company successfully moves to quash the subpoena or successfully asserts that the materials requested are privileged.

   It is often appropriate to meet with the government attorney or investigating agent to determine the proper scope of a subpoena and to clarify any ambiguities. These clarifications should be carefully documented with a memo to the file, and confirmed in writing with a letter to the government official negotiating the issue. Most often, the government is cooperative in amending the scope of the subpoena, especially if the terms of the subpoena reflect an inaccurate understanding of the recipient's business records and activities. In an extreme case, the company may need to resort to court action if the government is unwilling to negotiate.⁷

   b. **Appoint a Custodian**

   A document custodian should be appointed as soon as an investigation is under way. The custodian should be a person who is uninvolved in the underlying allegations. The appointment should be made in writing, and the custodian should be informed that the duties may require questioning under oath about the search and response to the subpoena. Sample instructions to a document custodian are attached at Tab 4. As a practical matter, it is generally better to appoint a non-lawyer employee to be responsible for the document search, so that the custodian is able to

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⁷ For a grand jury subpoena, a motion may be filed under Federal Rule of Criminal Procedure 17(c). For civil subpoenas, the company usually must await an enforcement action. Because agency and inspector general subpoenas (unlike grand jury subpoenas) are not self-enforcing, counsel should carefully document all of their efforts to negotiate the scope of the discovery demand. This documentation can be used to support the company's opposition, if the government seeks court-ordered enforcement of the subpoena.
testify about the search, if necessary. Normally, an in-house counsel should not act as document custodian because this may result in waiver of the attorney-client and work-product privileges.

c. **Provide Written Instructions to the Custodian and Searchers, Including Instructions Prohibiting the Destruction, Concealment, Alteration, or Fabrication of Relevant Documents**

All employees should be notified in writing that no potentially relevant documents are to be destroyed until the custodian, with assistance of counsel, has determined whether or not they are responsive. Corporate counsel cannot rely on oral instructions, and employees should receive clear written instructions that incorporate any understandings with the government. Sample instructions to company employees for responding to document requests and grand jury subpoenas are attached at Tabs 5 and 6.

Employees should be reminded that altering, destroying, concealing, or fabricating documents during a judicial or administrative proceeding, or criminal investigation or certain contemplated official proceedings could violate a number of federal laws, including the newly-enacted provisions of the Sarbanes-Oxley Act. Subpoenas are increasingly likely to apply to e-mail and other electronic information systems, and instructions to employees must include these forms of information if they are covered under the subpoena. Many companies now appoint an “electronic document custodian,” who is a person from the company’s IT department. This person is responsible for searching electronic files for responsive materials. Counsel should also review any automatic electronic mail deletion programs in place which could result in the deletion of relevant materials.

File search requests should also be in writing, and the custodian should document confirmations from individual employees that an appropriate search has been conducted and that all responsive documents have been produced. All documentation should be drafted with the
expectation that it may be produced to the government and will ultimately be provided to an investigating agency or grand jury.

The document search should be conducted throughout the company, wherever counsel or the corporate custodian reasonably believe responsive documents may be located. The custodian should have authority to gather documents from the highest level in the company. If no responsive documents have been found, this fact should also be documented. However, in many investigations, especially those that are driven by a subpoena or government demand, enormous numbers of documents may have to be produced.

d. **Provide for a Means of Establishing Objective Evidence of the Documents Produced**

The company has the right to review every document to determine whether a privilege applies; to number documents, including originals, with a Bates stamp; and to copy the documents that are produced. This avoids disputes over what was and what was not produced to the government. The document production should include a written cover letter setting forth the documents produced and the completeness of the response. This letter should be approved in advance by the appropriate member of corporate management and the document custodian. If some documents are not produced because they are privileged, the government routinely requires a privilege log.

B. **Communicating With Employees And Other Potential Witnesses**

Some of the most serious potential obstruction of justice issues can arise in dealings with witnesses, who are generally current or former corporate employees.

1. **Requests for Interviews -- the Witness' Rights**

*Unless compelled by a subpoena*, a person who is approached by a government investigator or auditor has the following rights:
• to speak or not to speak to the investigator, at the sole discretion of the witness;
• to condition any interview on any basis the person chooses, including, among other things:
  o the right to a personal attorney;
  o the right to be accompanied by corporate counsel or another company representative;
  o the right to discontinue the interview at any time;
  o the right to have the interview at the time and place of the person's own choosing;
  o the right to decide whether the interview is taped;
  o the right to advise the company before and after the interview of the interview request, the questions asked, and the responses given; and
  o the right to have a copy of the investigator's notes.

The corporate counsel has the right (and perhaps the duty) to notify its employee of these rights.\(^8\)

Preferably, such notice should be in writing to all affected employees at the start of an investigation so that the employees are not later confused as to the nature and content of the notice. In appropriate cases, it may be necessary to circulate that notice to large segments of the company. A copy of a generic notice is attached at Tab 7.

2. **Requests for Interviews -- the Corporate Counsel's Rights**

\(^8\) *But see* the Thompson Memorandum, which states that "[a]nother factor to be weighed [in assessing a corporation's level of cooperation with an investigation] 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 value of a corporation's cooperation. By the same token, the prosecutor should be wary of attempts to shield corporate officers and employees from liability by a willingness of the corporation to plead guilty." Thompson Memorandum at [ ]. In a footnote, the memorandum does acknowledge that state law may require the payment of legal fees in some circumstances, and that complying with local law "should not be considered a failure to cooperate." *Id.* n. 4.
Corporate counsel has the right to advise a company employee of the rights listed above. Under some circumstances, counsel may also advise an employee that they may retain their own counsel, at their own expense or at company expense. However, care must be taken to explain the right to reimbursement for legal fees under the company's corporate charter and state corporation laws, so that it is clear that payment of legal fees is not an inducement for testifying in a particular way. Counsel should also make it clear that payment of legal fees is not conditioned on the substance of the employee's testimony.

If separate representation is provided, corporate counsel has the right to:

- recommend (but not compel) a particular attorney to represent the employee;
- cooperate with the employee's attorney in preparation for the interview or testimony;
- review the expected questions and responses with the witness, if not separately represented;
- debrief the employee, if the employee agrees, after an interview or grand jury appearance; and
- limit the reimbursement of the employee’s counsel to “reasonable” legal fees and costs.

3. **Things Corporate Counsel Should Never Do:**

Corporate counsel should not:

- instruct an employee not to talk to or cooperate with an investigator or government attorney;
- give legal advice to the employee unless the corporate counsel is retained to represent the employee (a prospect that entails the risk of conflicts that are discussed below in Section C);
• advise the employee or a witness whom the counsel does not personally represent to exercise his or her Fifth Amendment right to refuse to answer questions;
• suggest or request that the employee give untruthful or evasive answers;
• threaten the witness with discharge or disciplinary action if the employee agrees to an interview with the government or testifies in a certain way.
4. **Things Corporate Counsel Should Do:**

Corporate counsel should:

- approach witness interviews with care, because the key participants may be either a leading government witness (i.e., a *qui tam* relator) or a potential target who may later cooperate with the prosecutor;
- tell the witness that, if they choose to testify, they should tell the truth; and
- notify the witness that any statement may be used against them or the company for criminal prosecution or other purposes.

C. **Interviewing, Preparing, and Debriefing Witnesses**

1. **Preparation for Testimony**

Interviewing, preparing, and debriefing witnesses is a very sensitive job, and can be fraught with danger from an obstruction standpoint. The corporate attorney generally should not represent current or former corporate employees, especially if the company (or the employee) is a subject or target of a government investigation. Retaining separate counsel for employee-witnesses helps to avoid ethical conflicts and allegations of obstruction or witness tampering. A corporate attorney who advises an employee to assert the Fifth Amendment in order to protect the company may violate 18 U.S.C. §§ 1503, 1505, 1510, or 1512.

Corporate counsel may, however, interview present and former employees as part of the corporation’s defense. Since the employee is part of the corporation, those interviews are privileged under both the attorney-client privilege and the work product doctrine. It is important that the employee witness (and the government investigator) understand that corporate counsel is representing the corporation, not the employee.
If the employee retains a personal attorney, corporate counsel may enter into a joint defense agreement ("JDA") with counsel for the employees, which can permit them to exchange information and legal and factual research without waiving privileges. Corporate counsel, who does not represent the witness, may participate in the witness preparation, but counsel should separately determine whether that should be done under an appropriate joint defense agreement. In most cases, corporate counsel has been involved longer in the investigation and has a greater knowledge of the facts and legal principles than counsel for the witness. These joint defense agreements, however, are much more problematic, particularly in cases in the Ninth Circuit.9 Great care should be taken in such cases.

When a witness is interviewed, there are a number of important rules to follow:

- If possible, conduct interviews with counsel and an additional witness (i.e., a paralegal or another attorney). The paralegal or second attorney should transcribe the notes. In most cases, an interested third party should not be permitted to sit in on the interview.
- The interview generally should begin with a written statement, establishing the reasons for the interview, whom the lawyer represents (making clear that corporate counsel represents the company, and not the individual employee), and the possible uses of the information gathered during the interview. The witness should be advised that the information provided by the employee at the interview

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9 In United States v. Henke, 222 F.3d 633 (9th Cir. 2000), the Ninth Circuit re-affirmed the validity of joint defense agreements, but the facts of this case highlight the ethical dilemmas that can arise under a JDA. In Henke, a former co-defendant, Gupta, pleaded guilty and testified at trial against the remaining defendants. Gupta's testimony was contradicted by earlier statements he had made during a joint defense meeting. Because counsel for the remaining defendants had an "implied" attorney-client relationship with the witness, they moved to withdraw from representing the remaining defendants in order to avoid the ethical violations inherent in using Gupta's confidences against him in cross-examination. The court denied the motion to withdraw, and counsel for the defendants were therefore put in the difficult position of choosing not to cross-examine the person who was now testifying for the government. See id. at 637-38.
is privileged as to the company, but the company may decide to waive the privilege and disclose the information to the government or to others. The written statement should be read verbatim so that there can be no dispute regarding the content of counsel's representations to the employee. Usually, a copy of that statement should be attached to the interview memorandum, if one is prepared. A sample opening statement is attached at Tab 8.

- In the normal case, an interview memorandum should be prepared. However, some government officials at a later date may insist on reviewing any interview memoranda that are prepared, so in some cases, it may not be best to prepare a memorandum of any kind. This memorandum, if one is prepared, usually should take care to state that it reflects the mental impressions of the attorney as well as the statements of the witness. If necessary to get the witness committed in writing, prepare a separate statement and do have the witness sign the interview memorandum.

- Most counsel prefer not to use tape or video recordings of interviews unless they are absolutely certain what an employee witness will say. Once that recording is made, it may be difficult or impossible to legally destroy it. In addition, many witnesses become far more circumspect when being recorded.

If a company employee refuses to cooperate with company counsel, the employee may be considered to have breached its fiduciary duty to cooperate with the company. (Some states, particularly California, have statutes that may require employee cooperation.) Failure to cooperate with a company investigation could subject the employee to discipline, including
termination. While such severe sanction is fraught with potential problems, the corporation taking adverse action should make the record clear on the following points:

- the employee is being disciplined or terminated for not cooperating in a legitimate investigation;
- the employee is not being terminated for “blowing the whistle” or cooperating with the government; and
- the employee is being told only to tell the full truth.

The employee should not be told that any statements made in the interview will not adversely affect the employee. After all, if the employee admits a crime or serious misconduct, the company should consider whether the employee should be fired (or at least put on leave) because of that conduct.

Preparing a witness for an interview or testimony to a federal official or grand jury should include:

- reviewing all relevant facts, including dates and persons involved;
- reviewing affidavits, correspondence, prior testimony, and other interviews conducted by the government;
- reviewing relevant legal principles, procurement regulations, rulings, court decisions, accounting principles, etc.; and
- emphasizing the need for truthful testimony.

2. **De-Briefing**

After the government interviews a witness, the witness may be debriefed by corporate counsel. This includes testimony before the grand jury, since grand jury secrecy rules apply only to the grand jurors and government personnel, and not to grand jury witnesses. However,
whether the witness cooperates with counsel is up to the witness, and there should not be any threats of sanctions for refusing a debriefing. (Note the difference between a debriefing and the initial interview. The employee should be required to disclose what happened, but not necessarily the government’s questions about what happened.) Corporate counsel may participate in a debriefing along with other attorneys or with employees counsel under an appropriate joint defense agreement. The debriefing may cover questions asked by the grand jury or in the interview, the responses given, and the documents reviewed.

D. Some Considerations that May Arise Following an Internal Investigation

The requirements imposed under the Securities and Exchange Commission's recently-released "Final Rule: Implementation of Standards of Professional Conduct for Attorneys" is properly the subject of another panel discussion. As a result, the SEC requirements are addressed only as a brief overview in these materials. However, attorneys conducting internal investigations for issuers may need to consider the new obligations that have been imposed under the Sarbanes-Oxley Act of 2002. Also discussed briefly below are considerations involved in making voluntary disclosures to the government.


Lawyers who appear and practice before the Securities and Exchange Commission\(^{10}\) are subject to "up-the-ladder" reporting requirements promulgated by the SEC under the Sarbanes-Oxley Act of 2002. The final rule, which was issued by the SEC on January 29, 2003 and takes effect on August 5, 2003,\(^{11}\) requires such attorneys to take the steps outlined below.

\(^{10}\) Conduct that constitutes "appearing and practicing before the Commission" is defined in the final rule, and is analyzed in a memorandum that is attached at Tab [x ] [attach Firm To Our Clients Memo only if JTB okays].

a. Evidence of a "material violation"\textsuperscript{12} of securities laws, of a breach of fiduciary duty, or other similar violations must be reported to the chief legal counsel or chief executive officer of an issuer. Alternatively, evidence of the violations described above may be reported to a "qualified legal compliance committee" ("QLCC") of the issuer. The QLCC would be responsible for, among other things, recommending the appropriate response to be taken by the issuer to evidence of a material violation. This alternative option applies only if the QLCC was in place before the incident for which it is being utilized.

b. If the chief legal officer or CEO fails to respond appropriately to the report, attorneys who don't report directly to a qualified legal compliance committee must report the evidence to i) the audit committee, ii) another committee of directors not employed by the issuer, or iii) directly to the board of directors.

c. Chief legal officers must investigate and take all reasonable steps necessary to enable the issuer to respond appropriately to the evidence of material violations.

The SEC generated a great deal of controversy when its proposed regulation included "noisy withdrawal" requirements. The noisy withdrawal proposals include two requirements: i) attorneys must withdraw from representing the client if up-the-ladder reporting did not result in an appropriate response from management or the board of directors; ii) the SEC must be notified (either by the attorney or by the issuer, in a public filing) of the noisy withdrawal. Recognizing the controversy that arose because of the noisy withdrawal requirements, the SEC has extended the comment period on this provision to April 7, 2003.

2. Reporting to the Government

\textsuperscript{12} Evidence of a material violation is defined as "credible evidence, based upon which it would be unreasonable, under the circumstances, for a prudent and competent attorney not to conclude that it is reasonably likely that a material violation has occurred, is ongoing, or is about to occur."
Some internal investigations will result in a voluntary disclosure or an oral or written report to the government. Counsel must be certain that factual statements in a voluntary disclosure are true and accurate. Witness interviews and documents must be available to support the statements, and the final report should be reviewed in advance and approved by responsible corporate officials. Be conservative, and if a fact cannot be established conclusively, say so. An intentional false statement may subject counsel to a charge under 18 U.S.C. § 1001 or an obstruction statute.
MEMORANDUM

TO: Heads of Department Components
   United States Attorneys

FROM: Larry D. Thompson
       Deputy Attorney General

SUBJECT: Principles of Federal Prosecution of Business Organizations

As the Corporate Fraud Task Force has advanced in its mission, we have confronted certain issues in the principles for the federal prosecution of business organizations that require revision in order to enhance our efforts against corporate fraud. While it will be a minority of cases in which a corporation or partnership is itself subjected to criminal charges, prosecutors and investigators in every matter involving business crimes must assess the merits of seeking the conviction of the business entity itself.

Attached to this memorandum are a revised set of principles to guide Department prosecutors as they make the decision whether to seek charges against a business organization. These revisions draw heavily on the combined efforts of the Corporate Fraud Task Force and the Attorney General's Advisory Committee to put the results of more than three years of experience with the principles into practice.

The main focus of the revisions is increased emphasis on and scrutiny of the authenticity of a corporation's cooperation. Too often business organizations, while purporting to cooperate with a Department investigation, in fact take steps to impede the quick and effective exposure of the complete scope of wrongdoing under investigation. The revisions make clear that such conduct should weigh in favor of a corporate prosecution. The revisions also address the efficacy of the corporate governance mechanisms in place within a corporation, to ensure that these measures are truly effective rather than mere paper programs.

Further experience with these principles may lead to additional adjustments. I look forward to hearing comments about their operation in practice. Please forward any comments to Christopher Wray, the Principal Associate Deputy Attorney General, or to Andrew Hruska, my Senior Counsel.
Federal Prosecution of Business Organizations

I. Charging a Corporation: General

A. General Principle: Corporations should not be treated leniently because of their artificial nature nor should they be subject to harsher treatment. Vigorous enforcement of the criminal laws against corporate wrongdoers, where appropriate results in great benefits for law enforcement and the public, particularly in the area of white collar crime. Indicting corporations for wrongdoing enables the government to address and be a force for positive change of corporate culture, alter corporate behavior, and prevent, discover, and punish white collar crime.

B. Comment: In all cases involving corporate wrongdoing, prosecutors should consider the factors discussed herein. First and foremost, prosecutors should be aware of the important public benefits that may flow from indicting a corporation in appropriate cases. For instance, corporations are likely to take immediate remedial steps when one is indicted for criminal conduct that is pervasive throughout a particular industry, and thus an indictment often provides a unique opportunity for deterrence on a massive scale. In addition, a corporate indictment may result in specific deterrence by changing the culture of the indicted corporation and the behavior of its employees. Finally, certain crimes that carry with them a substantial risk of great public harm, e.g., environmental crimes or financial frauds, are by their nature most likely to be committed by businesses, and there may, therefore, be a substantial federal interest in indicting the corporation.

Charging a corporation, however, does not mean that individual directors, officers, employees, or shareholders should not also be charged. Prosecution of a corporation is not a substitute for the prosecution of criminally culpable individuals within or without the corporation. Because a corporation can act only through individuals, imposition of individual criminal liability may provide the strongest deterrent against future corporate wrongdoing. Only rarely should provable individual culpability not be pursued, even in the face of offers of corporate guilty pleas.

Corporations are "legal persons," capable of suing and being sued, and capable of committing crimes. Under the doctrine of respondeat superior, a corporation may be held criminally liable for the illegal acts of its directors, officers, employees, and agents. To hold a corporation liable for these actions, the government must establish that the corporate agent's actions (i) were within the scope of his duties and (ii) were intended, at least in part, to benefit the corporation. In all cases involving wrongdoing by corporate agents, prosecutors should consider the corporation, as well as the responsible individuals, as potential criminal targets.

Agents, however, may act for mixed reasons -- both for self-aggrandizement (both direct and indirect) and for the benefit of the corporation, and a corporation may be held liable as long as one motivation of its agent is to benefit the corporation. In United States v. Automated Medical Laboratories, 770 F.2d 399 (4th Cir. 1985), the court affirmed the corporation's conviction for the actions of a subsidiary's employee despite its claim that the employee was acting for his own benefit, namely his "ambitious nature and his desire to ascend the corporate ladder." The court stated, "Partucci was clearly acting in part to benefit AML since his advancement within the corporation depended on AML's well-being and its lack of difficulties with the FDA." Similarly, in United States v. Cincotta, 689 F.2d 238, 241-42 (1st Cir. 1982), the court held, "criminal liability may be imposed on the corporation only where the agent is acting
within the scope of his employment. That, in turn, requires that the agent be performing acts of
the kind which he is authorized to perform, and those acts must be motivated -- at least in part --
by an intent to benefit the corporation." Applying this test, the court upheld the corporation's
conviction, notwithstanding the substantial personal benefit reaped by its miscreant agents,
because the fraudulent scheme required money to pass through the corporation's treasury and the
fraudulently obtained goods were resold to the corporation's customers in the corporation's name.
As the court concluded, "Mystic--not the individual defendants--was making money by selling
oil that it had not paid for."

Moreover, the corporation need not even necessarily profit from its agent's actions for it to
be held liable. In Automated Medical Laboratories, the Fourth Circuit stated:

[B]enefit is not a "touchstone of criminal corporate liability; benefit at best is an
evidential, not an operative, fact." Thus, whether the agent's actions ultimately
redounded to the benefit of the corporation is less significant than whether the agent
acted with the intent to benefit the corporation. The basic purpose of requiring that an
agent have acted with the intent to benefit the corporation, however, is to insulate the
corporation from criminal liability for actions of its agents which be inimical to the
interests of the corporation or which may have been undertaken solely to advance the
interests of that agent or of a party other than the corporation.

770 F.2d at 407 (emphasis added; quoting Old Monastery Co. v. United States, 147 F.2d 905,
908 (4th Cir.), cert. denied, 326 U.S. 734 (1945)).

II. Charging a Corporation: Factors to Be Considered

A. General Principle: Generally, prosecutors should apply the same factors in determining
whether to charge a corporation as they do with respect to individuals. See USAM § 9-27.220, et seq.
Thus, the prosecutor should weigh all of the factors normally considered in the sound
exercise of prosecutorial judgment: the sufficiency of the evidence; the likelihood of success at
trial; the probable deterrent, rehabilitative, and other consequences of conviction; and the
adequacy of noncriminal approaches. See id. However, due to the nature of the corporate
"person," some additional factors are present. In conducting an investigation, determining
whether to bring charges, and negotiating plea agreements, prosecutors should consider the
following factors in reaching a decision as to the proper treatment of a corporate target:

1. the nature and seriousness of the offense, including the risk of harm to the public, and
applicable policies and priorities, if any, governing the prosecution of corporations for
particular categories of crime (see section III, infra);

2. the pervasiveness of wrongdoing within the corporation, including the complicity in, or
condonation of, the wrongdoing by corporate management (see section IV, infra);

3. the corporation's history of similar conduct, including prior criminal, civil, and
regulatory enforcement actions against it (see section V, infra);

4. the corporation's timely and voluntary disclosure of wrongdoing and its willingness to
cooperate in the investigation of its agents, including, if necessary, the waiver of corporate
attorney-client and work product protection (*see* section VI, *infra*);

5. the existence and adequacy of the corporation's compliance program (*see* section VII, *infra*);

6. the corporation’s remedial actions, including any efforts to implement an effective corporate compliance program or to improve an existing one, to replace responsible management, to discipline or terminate wrongdoers, to pay restitution, and to cooperate with the relevant government agencies (*see* section VIII, *infra*);

7. collateral consequences, including disproportionate harm to shareholders, pension holders and employees not proven personally culpable and impact on the public arising from the prosecution (*see* section IX, *infra*); and

8. the adequacy of the prosecution of individuals responsible for the corporation's malfeasance;

9. the adequacy of remedies such as civil or regulatory enforcement actions (*see* section X, *infra*).

B. Comment: As with the factors relevant to charging natural persons, the foregoing factors are intended to provide guidance rather than to mandate a particular result. The factors listed in this section are intended to be illustrative of those that should be considered and not a complete or exhaustive list. Some or all of these factors may or may not apply to specific cases, and in some cases one factor may override all others. The nature and seriousness of the offense may be such as to warrant prosecution regardless of the other factors. Further, national law enforcement policies in various enforcement areas may require that more or less weight be given to certain of these factors than to others.

In making a decision to charge a corporation, the prosecutor generally has wide latitude in determining when, whom, how, and even whether to prosecute for violations of Federal criminal law. In exercising that discretion, prosecutors should consider the following general statements of principles that summarize appropriate considerations to be weighed and desirable practices to be followed in discharging their prosecutorial responsibilities. In doing so, prosecutors should ensure that the general purposes of the criminal law -- assurance of warranted punishment, deterrence of further criminal conduct, protection of the public from dangerous and fraudulent conduct, rehabilitation of offenders, and restitution for victims and affected communities -- are adequately met, taking into account the special nature of the corporate "person."

III. Charging a Corporation: Special Policy Concerns

A. General Principle: The nature and seriousness of the crime, including the risk of harm to the public from the criminal conduct, are obviously primary factors in determining whether to charge a corporation. In addition, corporate conduct, particularly that of national and multinational corporations, necessarily intersects with federal economic, taxation, and criminal law enforcement policies. In applying these principles, prosecutors must consider the practices and policies of the appropriate Division of the Department, and must comply with those policies to the extent required.
B. Comment: In determining whether to charge a corporation, prosecutors should take into account federal law enforcement priorities as discussed above. See USAM § 9-27-230. In addition, however, prosecutors must be aware of the specific policy goals and incentive programs established by the respective Divisions and regulatory agencies. Thus, whereas natural persons may be given incremental degrees of credit (ranging from immunity to lesser charges to sentencing considerations) for turning themselves in, making statements against their penal interest, and cooperating in the government's investigation of their own and others' wrongdoing, the same approach may not be appropriate in all circumstances with respect to corporations. As an example, it is entirely proper in many investigations for a prosecutor to consider the corporation's pre-indictment conduct, e.g., voluntary disclosure, cooperation, remediation or restitution, in determining whether to seek an indictment. However, this would not necessarily be appropriate in an antitrust investigation, in which antitrust violations, by definition, go to the heart of the corporation's business and for which the Antitrust Division has therefore established a firm policy, understood in the business community, that credit should not be given at the charging stage for a compliance program and that amnesty is available only to the first corporation to make full disclosure to the government. As another example, the Tax Division has a strong preference for prosecuting responsible individuals, rather than entities, for corporate tax offenses. Thus, in determining whether or not to charge a corporation, prosecutors should consult with the Criminal, Antitrust, Tax, and Environmental and Natural Resources Divisions, if appropriate or required.

IV. Charging a Corporation: Pervasiveness of Wrongdoing Within the Corporation

A. General Principle: A corporation can only act through natural persons, and it is therefore held responsible for the acts of such persons fairly attributable to it. Charging a corporation for even minor misconduct may be appropriate where the wrongdoing was pervasive and was undertaken by a large number of employees or by all the employees in a particular role within the corporation, e.g., salesmen or procurement officers, or was condoned by upper management. On the other hand, in certain limited circumstances, it may not be appropriate to impose liability upon a corporation, particularly one with a compliance program in place, under a strict respondeat superior theory for the single isolated act of a rogue employee. There is, of course, a wide spectrum between these two extremes, and a prosecutor should exercise sound discretion in evaluating the pervasiveness of wrongdoing within a corporation.

B. Comment: Of these factors, the most important is the role of management. Although acts of even low-level employees may result in criminal liability, a corporation is directed by its management and management is responsible for a corporate culture in which criminal conduct is either discouraged or tacitly encouraged. As stated in commentary to the Sentencing Guidelines: Pervasiveness [is] case specific and [will] depend on the number, and degree of responsibility, of individuals [with] substantial authority . . . who participated in, condoned, or were willfully ignorant of the offense. Fewer individuals need to be involved for a finding of pervasiveness if those individuals exercised a relatively high degree of authority. Pervasiveness can occur either within an organization as a whole or within a unit of an organization. USSG §8C2.5, comment. (n. 4).

V. Charging a Corporation: The Corporation's Past History
A. General Principle: Prosecutors may consider a corporation's history of similar conduct, including prior criminal, civil, and regulatory enforcement actions against it, in determining whether to bring criminal charges.

B. Comment: A corporation, like a natural person, is expected to learn from its mistakes. A history of similar conduct may be probative of a corporate culture that encouraged, or at least condoned, such conduct, regardless of any compliance programs. Criminal prosecution of a corporation may be particularly appropriate where the corporation previously had been subject to non-criminal guidance, warnings, or sanctions, or previous criminal charges, and yet it either had not taken adequate action to prevent future unlawful conduct or had continued to engage in the conduct in spite of the warnings or enforcement actions taken against it. In making this determination, the corporate structure itself, e.g., subsidiaries or operating divisions, should be ignored, and enforcement actions taken against the corporation or any of its divisions, subsidiaries, and affiliates should be considered. See USSG § 8C2.5(c) & comment. (n. 6).

VI. Charging a Corporation: Cooperation and Voluntary Disclosure

A. General Principle: In 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. 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.

B. Comment: In investigating wrongdoing by or within a corporation, a prosecutor is likely to encounter several obstacles resulting from the nature of the corporation itself. It will often be difficult to determine which individual took which action on behalf of the corporation. Lines of authority and responsibility may be shared among operating divisions or departments, and records and personnel may be spread throughout the United States or even among several countries. Where the criminal conduct continued over an extended period of time, the culpable or knowledgeable personnel may have been promoted, transferred, or fired, or they may have quit or retired. Accordingly, a corporation's cooperation may be critical in identifying the culprits and locating relevant evidence.

In some circumstances, therefore, granting a corporation immunity or amnesty or pretrial diversion may be considered in the course of the government's investigation. In such circumstances, prosecutors should refer to the principles governing non-prosecution agreements generally. See USAM § 9-27.600-650. These principles permit a non-prosecution agreement in exchange for cooperation when a corporation's "timely cooperation appears to be necessary to the public interest and other means of obtaining the desired cooperation are unavailable or would not be effective." Prosecutors should note that in the case of national or multi-national corporations, multi-district or global agreements may be necessary. Such agreements may only be entered into with the approval of each affected district or the appropriate Department official. See USAM §9-27.641.

In addition, the Department, in conjunction with regulatory agencies and other executive branch departments, encourages corporations, as part of their compliance programs, to conduct
internal investigations and to disclose their findings to the appropriate authorities. Some agencies, such as the SEC and the EPA, as well as the Department's Environmental and Natural Resources Division, have formal voluntary disclosure programs in which self-reporting, coupled with remediation and additional criteria, may qualify the corporation for amnesty or reduced sanctions. Even in the absence of a formal program, prosecutors may consider a corporation's timely and voluntary disclosure in evaluating the adequacy of the corporation's compliance program and its management's commitment to the compliance program. However, prosecution and economic policies specific to the industry or statute may require prosecution notwithstanding a corporation's willingness to cooperate. For example, the Antitrust Division offers amnesty only to the first corporation to agree to cooperate. This creates a strong incentive for corporations participating in anti-competitive conduct to be the first to cooperate. In addition, amnesty, immunity, or reduced sanctions may not be appropriate where the corporation's business is permeated with fraud or other crimes.

One factor the prosecutor may weigh in assessing the adequacy of a corporation's cooperation is the completeness of its disclosure including, if necessary, a waiver of the attorney-client and work product protections, both with respect to its internal investigation and with respect to communications between specific officers, directors and employees and counsel. Such waivers permit the government to obtain statements of possible witnesses, subjects, and targets, without having to negotiate individual cooperation or immunity agreements. In addition, they are often critical in enabling the government to evaluate the completeness of a corporation's voluntary disclosure and cooperation. Prosecutors may, therefore, request a waiver in appropriate circumstances. The Department does not, however, consider waiver of a corporation's attorney-client and work product protection an absolute requirement, and prosecutors should consider the willingness of a corporation to waive such protection when necessary to provide timely and complete information as one factor in evaluating the corporation's cooperation.

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 value of a corporation's cooperation. By the same token, the prosecutor should be wary of attempts to shield corporate officers and employees from liability by a willingness of the corporation to plead guilty.

Another factor to be weighed by the prosecutor is whether the corporation, while purporting to cooperate, has engaged in conduct that impedes the investigation (whether or not rising to the level of criminal obstruction). Examples of such conduct include: overly broad assertions of corporate representation of employees or former employees; inappropriate directions to employees or their counsel, such as directions not to cooperate openly and fully with the investigation including, for example, the direction to decline to be interviewed; making presentations or submissions that contain misleading assertions or omissions; incomplete or delayed production of records; and failure to promptly disclose illegal conduct known to the corporation.
Finally, a corporation's offer of cooperation does not automatically entitle it to immunity from prosecution. A corporation should not be able to escape liability merely by offering up its directors, officers, employees, or agents as in lieu of its own prosecution. Thus, a corporation's willingness to cooperate is merely one relevant factor, that needs to be considered in conjunction with the other factors, particularly those relating to the corporation's past history and the role of management in the wrongdoing.

VII. Charging a Corporation: Corporate Compliance Programs

A. General Principle: Compliance programs are established by corporate management to prevent and to detect misconduct and to ensure that corporate activities are conducted in accordance with all applicable criminal and civil laws, regulations, and rules. The Department encourages such corporate self-policing, including voluntary disclosures to the government of any problems that a corporation discovers on its own. However, the existence of a compliance program is not sufficient, in and of itself, to justify not charging a corporation for criminal conduct undertaken by its officers, directors, employees, or agents. Indeed, the commission of such crimes in the face of a compliance program may suggest that the corporate management is not adequately enforcing its program. In addition, the nature of some crimes, e.g., antitrust violations, may be such that national law enforcement policies mandate prosecutions of corporations notwithstanding the existence of a compliance program.

B. Comment: A corporate compliance program, even one specifically prohibiting the very conduct in question, does not absolve the corporation from criminal liability under the doctrine of respondeat superior. See United States v. Basic Construction Co., 711 F.2d 570 (4th Cir. 1983) ("a corporation may be held criminally responsible for antitrust violations committed by its employees if they were acting within the scope of their authority, or apparent authority, and for the benefit of the corporation, even if . . . such acts were against corporate policy or express instructions."). In United States v. Hilton Hotels Corp., 467 F.2d 1000 (9th Cir. 1972), cert. denied, 409 U.S. 1125 (1973), the Ninth Circuit affirmed antitrust liability based upon a purchasing agent for a single hotel threatening a single supplier with a boycott unless it paid dues to a local marketing association, even though the agent's actions were contrary to corporate policy and directly against express instructions from his superiors. The court reasoned that Congress, in enacting the Sherman Antitrust Act, "intended to impose liability upon business entities for the acts of those to whom they choose to delegate the conduct of their affairs, thus stimulating a maximum effort by owners and managers to assure adherence by such agents to the requirements of the Act." It concluded that "general policy statements" and even direct instructions from the agent's superiors were not sufficient; "Appellant could not gain exculpation by issuing general instructions without undertaking to enforce those instructions by means commensurate with the obvious risks." See also United States v. Beusch, 596 F.2d 871, 878 (9th Cir. 1979) ("[A] corporation may be liable for the acts of its employees done contrary to express instructions and policies, but . . . the existence of such instructions and policies may be considered in determining whether the employee in fact acted to benefit the corporation."); United States v. American Radiator & Standard Sanitary Corp., 433 F.2d 174 (3rd Cir. 1970) (affirming conviction of corporation based upon its officer's participation in price-fixing scheme, despite corporation's defense that officer's conduct violated its "rigid anti-fraternization policy" against any socialization (and exchange of price information) with its competitors; "When the act of the agent is within the scope of his employment or his apparent authority, the corporation is
While the Department recognizes that no compliance program can ever prevent all
criminal activity by a corporation's employees, the critical factors in evaluating any program are
whether the program is adequately designed for maximum effectiveness in preventing and
detecting wrongdoing by employees and whether corporate management is enforcing the
program or is tacitly encouraging or pressuring employees to engage in misconduct to achieve
business objectives. The Department has no formal guidelines for corporate compliance
programs. The fundamental questions any prosecutor should ask are: "Is the corporation's
compliance program well designed?" and "Does the corporation's compliance program work?"
In answering these questions, the prosecutor should consider the comprehensiveness of the
compliance program; the extent and pervasiveness of the criminal conduct; the number and level
of the corporate employees involved; the seriousness, duration, and frequency of the misconduct;
and any remedial actions taken by the corporation, including restitution, disciplinary action, and
revisions to corporate compliance programs. Prosecutors should also consider the promptness
of any disclosure of wrongdoing to the government and the corporation's cooperation in the
government's investigation. In evaluating compliance programs, prosecutors may consider
whether the corporation has established corporate governance mechanisms that can effectively
detect and prevent misconduct. For example, do the corporation's directors exercise independent
review over proposed corporate actions rather than unquestioningly ratifying officers' recomendations; are the directors provided with information sufficient to enable the exercise of independent judgment, are internal audit functions conducted at a level sufficient to ensure their independence and accuracy and have the directors established an information and reporting system in the organization reasonable designed to provide management and the board of directors with timely and accurate information sufficient to allow them to reach an informed decision regarding the organization's compliance with the law. In re: Caremark, 698 A.2d 959 (Del. Ct. Chan. 1996).

Prosecutors should therefore attempt to determine whether a corporation's compliance
program is merely a "paper program" or whether it was designed and implemented in an
effective manner. In addition, prosecutors should determine whether the corporation has
provided for a staff sufficient to audit, document, analyze, and utilize the results of the
corporation's compliance efforts. In addition, prosecutors should determine whether the
 corporation's employees are adequately informed about the compliance program and are
convinced of the corporation's commitment to it. This will enable the prosecutor to make an
informed decision as to whether the corporation has adopted and implemented a truly effective
compliance program that, when consistent with other federal law enforcement policies, may
result in a decision to charge only the corporation's employees and agents.

Compliance programs should be designed to detect the particular types of misconduct
most likely to occur in a particular corporation's line of business. Many corporations operate in
complex regulatory environments outside the normal experience of criminal prosecutors.
Accordingly, prosecutors should consult with relevant federal and state agencies with the
expertise to evaluate the adequacy of a program's design and implementation. For instance, state
and federal banking, insurance, and medical boards, the Department of Defense, the Department
of Health and Human Services, the Environmental Protection Agency, and the Securities and
Exchange Commission have considerable experience with compliance programs and can be very
helpful to a prosecutor in evaluating such programs. In addition, the Fraud Section of the Criminal Division, the Commercial Litigation Branch of the Civil Division, and the Environmental Crimes Section of the Environment and Natural Resources Division can assist U.S. Attorneys' Offices in finding the appropriate agency office and in providing copies of compliance programs that were developed in previous cases.

VIII. Charging a Corporation: Restitution and Remediation

A. General Principle: Although neither a corporation nor an individual target may avoid prosecution merely by paying a sum of money, a prosecutor may consider the corporation's willingness to make restitution and steps already taken to do so. A prosecutor may also consider other remedial actions, such as implementing an effective corporate compliance program, improving an existing compliance program, and disciplining wrongdoers, in determining whether to charge the corporation.

B. Comment: In determining whether or not a corporation should be prosecuted, a prosecutor may consider whether meaningful remedial measures have been taken, including employee discipline and full restitution. A corporation's response to misconduct says much about its willingness to ensure that such misconduct does not recur. Thus, corporations that fully recognize the seriousness of their misconduct and accept responsibility for it should be taking steps to implement the personnel, operational, and organizational changes necessary to establish an awareness among employees that criminal conduct will not be tolerated. Among the factors prosecutors should consider and weigh are whether the corporation appropriately disciplined the wrongdoers and disclosed information concerning their illegal conduct to the government.

Employee discipline is a difficult task for many corporations because of the human element involved and sometimes because of the seniority of the employees concerned. While corporations need to be fair to their employees, they must also be unequivocally committed, at all levels of the corporation, to the highest standards of legal and ethical behavior. Effective internal discipline can be a powerful deterrent against improper behavior by a corporation's employees. In evaluating a corporation's response to wrongdoing, prosecutors may evaluate the willingness of the corporation to discipline culpable employees of all ranks and the adequacy of the discipline imposed. The prosecutor should be satisfied that the corporation's focus is on the integrity and credibility of its remedial and disciplinary measures rather than on the protection of the wrongdoers.

In addition to employee discipline, two other factors used in evaluating a corporation's remedial efforts are restitution and reform. As with natural persons, the decision whether or not to prosecute should not depend upon the target's ability to pay restitution. A corporation's efforts to pay restitution even in advance of any court order is, however, evidence of its "acceptance of responsibility" and, consistent with the practices and policies of the appropriate Division of the Department entrusted with enforcing specific criminal laws, may be considered in determining whether to bring criminal charges. Similarly, although the inadequacy of a corporate compliance program is a factor to consider when deciding whether to charge a corporation, that corporation's quick recognition of the flaws in the program and its efforts to improve the program are also factors to consider.

IX. Charging a Corporation: Collateral Consequences
A. General Principle: Prosecutors may consider the collateral consequences of a corporate criminal conviction in determining whether to charge the corporation with a criminal offense.

B. Comment: One of the factors in determining whether to charge a natural person or a corporation is whether the likely punishment is appropriate given the nature and seriousness of the crime. In the corporate context, prosecutors may take into account the possibly substantial consequences to a corporation's officers, directors, employees, and shareholders, many of whom may, depending on the size and nature (e.g., publicly vs. closely held) of the corporation and their role in its operations, have played no role in the criminal conduct, have been completely unaware of it, or have been wholly unable to prevent it. Prosecutors should also be aware of non-penal sanctions that may accompany a criminal charge, such as potential suspension or debarment from eligibility for government contracts or federal funded programs such as health care. Whether or not such non-penal sanctions are appropriate or required in a particular case is the responsibility of the relevant agency, a decision that will be made based on the applicable statutes, regulations, and policies.

Virtually every conviction of a corporation, like virtually every conviction of an individual, will have an impact on innocent third parties, and the mere existence of such an effect is not sufficient to preclude prosecution of the corporation. Therefore, in evaluating the severity of collateral consequences, various factors already discussed, such as the pervasiveness of the criminal conduct and the adequacy of the corporation's compliance programs, should be considered in determining the weight to be given to this factor. For instance, the balance may tip in favor of prosecuting corporations in situations where the scope of the misconduct in a case is widespread and sustained within a corporate division (or spread throughout pockets of the corporate organization). In such cases, the possible unfairness of visiting punishment for the corporation's crimes upon shareholders may be of much less concern where those shareholders have substantially profited, even unknowingly, from widespread or pervasive criminal activity. Similarly, where the top layers of the corporation's management or the shareholders of a closely-held corporation were engaged in or aware of the wrongdoing and the conduct at issue was accepted as a way of doing business for an extended period, debarment may be deemed not collateral, but a direct and entirely appropriate consequence of the corporation's wrongdoing. The appropriateness of considering such collateral consequences and the weight to be given them may depend on the special policy concerns discussed in section III, supra.

X. Charging a Corporation: Non-Criminal Alternatives

A. General Principle: Although non-criminal alternatives to prosecution often exist, prosecutors may consider whether such sanctions would adequately deter, punish, and rehabilitate a corporation that has engaged in wrongful conduct. In evaluating the adequacy of non-criminal alternatives to prosecution, e.g., civil or regulatory enforcement actions, the prosecutor may consider all relevant factors, including:

1. the sanctions available under the alternative means of disposition;

2. the likelihood that an effective sanction will be imposed; and
3. the effect of non-criminal disposition on Federal law enforcement interests.

B. Comment: The primary goals of criminal law are deterrence, punishment, and rehabilitation. Non-criminal sanctions may not be an appropriate response to an egregious violation, a pattern of wrongdoing, or a history of non-criminal sanctions without proper remediation. In other cases, however, these goals may be satisfied without the necessity of instituting criminal proceedings. In determining whether federal criminal charges are appropriate, the prosecutor should consider the same factors (modified appropriately for the regulatory context) considered when determining whether to leave prosecution of a natural person to another jurisdiction or to seek non-criminal alternatives to prosecution. These factors include: the strength of the regulatory authority's interest; the regulatory authority's ability and willingness to take effective enforcement action; the probable sanction if the regulatory authority's enforcement action is upheld; and the effect of a non-criminal disposition on Federal law enforcement interests. See USAM §§ 9-27.240, 9-27.250.

XI. Charging a Corporation: Selecting Charges

A. General Principle: Once a prosecutor has decided to charge a corporation, the prosecutor should charge, or should recommend that the grand jury charge, the most serious offense that is consistent with the nature of the defendant's conduct and that is likely to result in a sustainable conviction.

B. Comment: Once the decision to charge is made, the same rules as govern charging natural persons apply. These rules require "a faithful and honest application of the Sentencing Guidelines" and an "individualized assessment of the extent to which particular charges fit the specific circumstances of the case, are consistent with the purposes of the Federal criminal code, and maximize the impact of Federal resources on crime." See USAM § 9-27.300. In making this determination, "it is appropriate that the attorney for the government consider, inter alia, such factors as the sentencing guideline range yielded by the charge, whether the penalty yielded by such sentencing range . . . is proportional to the seriousness of the defendant's conduct, and whether the charge achieves such purposes of the criminal law as punishment, protection of the public, specific and general deterrence, and rehabilitation." See Attorney General's Memorandum, dated October 12, 1993.

XII. Plea Agreements with Corporations

A. General Principle: In negotiating plea agreements with corporations, prosecutors should seek a plea to the most serious, readily provable offense charged. In addition, the terms of the plea agreement should contain appropriate provisions to ensure punishment, deterrence, rehabilitation, and compliance with the plea agreement in the corporate context. Although special circumstances may mandate a different conclusion, prosecutors generally should not agree to accept a corporate guilty plea in exchange for non-prosecution or dismissal of charges against individual officers and employees.

B. Comment: Prosecutors may enter into plea agreements with corporations for the same reasons and under the same constraints as apply to plea agreements with natural persons. See USAM §§ 9-27.400-500. This means, inter alia, that the corporation should be required to plead guilty to the most serious, readily provable offense charged. As is the case with
individuals, the attorney making this determination should do so "on the basis of an individualized assessment of the extent to which particular charges fit the specific circumstances of the case, are consistent with the purposes of the federal criminal code, and maximize the impact of federal resources on crime. In making this determination, the attorney for the government considers, inter alia, such factors as the sentencing guideline range yielded by the charge, whether the penalty yielded by such sentencing range . . . is proportional to the seriousness of the defendant's conduct, and whether the charge achieves such purposes of the criminal law as punishment, protection of the public, specific and general deterrence, and rehabilitation." See Attorney General's Memorandum, dated October 12, 1993. In addition, any negotiated departures from the Sentencing Guidelines must be justifiable under the Guidelines and must be disclosed to the sentencing court. A corporation should be made to realize that pleading guilty to criminal charges constitutes an admission of guilt and not merely a resolution of an inconvenient distraction from its business. As with natural persons, pleas should be structured so that the corporation may not later "proclaim lack of culpability or even complete innocence." See USAM §§ 9-27.420(b)(4), 9-27.440, 9-27.500. Thus, for instance, there should be placed upon the record a sufficient factual basis for the plea to prevent later corporate assertions of innocence.

A corporate plea agreement should also contain provisions that recognize the nature of the corporate "person" and ensure that the principles of punishment, deterrence, and rehabilitation are met. In the corporate context, punishment and deterrence are generally accomplished by substantial fines, mandatory restitution, and institution of appropriate compliance measures, including, if necessary, continued judicial oversight or the use of special masters. See USSG §§ 8B1.1, 8C2.1, et seq. In addition, where the corporation is a government contractor, permanent or temporary debarment may be appropriate. Where the corporation was engaged in government contracting fraud, a prosecutor may not negotiate away an agency's right to debar or to list the corporate defendant.

In negotiating a plea agreement, prosecutors should also consider the deterrent value of prosecutions of individuals within the corporation. Therefore, one factor that a prosecutor may consider in determining whether to enter into a plea agreement is whether the corporation is seeking immunity for its employees and officers or whether the corporation is willing to cooperate in the investigation of culpable individuals. Prosecutors should rarely negotiate away individual criminal liability in a corporate plea.

Rehabilitation, of course, requires that the corporation undertake to be law-abiding in the future. It is, therefore, appropriate to require the corporation, as a condition of probation, to implement a compliance program or to reform an existing one. As discussed above, prosecutors may consult with the appropriate state and federal agencies and components of the Justice Department to ensure that a proposed compliance program is adequate and meets industry standards and best practices. See section VII, supra.

In plea agreements in which the corporation agrees to cooperate, the prosecutor should ensure that the cooperation is complete and truthful. To do so, the prosecutor may request that the corporation waive attorney-client and work product protection, make employees and agents available for debriefing, disclose the results of its internal investigation, file appropriate certified financial statements, agree to governmental or third-party audits, and take whatever other steps are necessary to ensure that the full scope of the corporate wrongdoing is disclosed and that the
responsible culprits are identified and, if appropriate, prosecuted. See generally section VIII, supra.

Footnotes:

1. While these guidelines refer to corporations, they apply to the consideration of the prosecution of all types of business organizations, including partnerships, sole proprietorships, government entities, and unincorporated associations.

2. In addition, the Sentencing Guidelines reward voluntary disclosure and cooperation with a reduction in the corporation's offense level. See USSG §8C2.5).

3. This 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.

4. Some states require corporations to pay the legal fees of officers under investigation prior to a formal determination of their guilt. Obviously, a corporation's compliance with governing law should not be considered a failure to cooperate.

5. Although this case and Basic Construction are both antitrust cases, their reasoning applies to other criminal violations. In the Hilton case, for instance, the Ninth Circuit noted that Sherman Act violations are commercial offenses "usually motivated by a desire to enhance profits," thus, bringing the case within the normal rule that a "purpose to benefit the corporation is necessary to bring the agent's acts within the scope of his employment." 467 F.2d at 1006 & n4. In addition, in United States v. Automated Medical Laboratories, 770 F.2d 399, 406 n.5 (4th Cir. 1985), the Fourth Circuit stated "that Basic Construction states a generally applicable rule on corporate criminal liability despite the fact that it addresses violations of the antitrust laws."

6. For a detailed review of these and other factors concerning corporate compliance programs, see United States Sentencing Commission, GUIDELINES MANUAL, §8A1.2, comment. (n.3(k)) (Nov. 1997). See also USSG §8C2.5(f)

7. For example, the Antitrust Division's amnesty policy requires that "[w]here possible, the corporation [make] restitution to injured parties...."
Section 802. Criminal Penalties for Altering Documents

*Previous law:* Prior to the Sarbanes-Oxley Act of 2002, anyone who "corruptly persuades" others to destroy, alter or conceal evidence can be prosecuted under 18 U.S.C. § 1512. Section 1512 reaches destruction of evidence with intent to obstruct an official proceeding which may not yet have been commenced. However, Section 1512 does not reach the "individual shredder." While prosecution of obstruction under 18 U.S.C. § 1505 does not require "corrupt persuasion," it does require the existence of a pending proceeding. In addition, existing law does not explicitly address the retention of accounting work papers for a fixed period of time.

*Amendment:* Section 802 adds two new criminal provisions, 18 U.S.C. §§ 1519 and 1520. Section 1519 expands existing law to cover the alteration, destruction or falsification of records, documents or tangible objects, by any person, with intent to impede, obstruct or influence, the investigation or proper administration of any "matters" within the jurisdiction of any department or agency of the United States, or any bankruptcy proceeding, or in relation to or contemplation of any such matter or proceeding. This section explicitly reaches activities by an individual "in relation to or contemplation of" any matters. No corrupt persuasion is required. New Section 1519 should be read in conjunction with the amendment to 18 U.S.C. 1512 added by Section 1102 of this Act, discussed below, which similarly bars corrupt acts to destroy, alter, mutilate or conceal evidence, in contemplation of an "official proceeding."

Accountants who fail to retain the audit or review workpapers of a covered audit for a period of 5 years will violate Section 1520, which creates a new felony, with a maximum period of incarceration of ten years. Under rulemaking authority granted in Section 1520(b), the SEC will promulgate rules relating to the retention of workpapers and other audit or review documents.

New 18 U.S.C. § 1519 provides:

*Whoever knowingly alters, destroys, mutilates, conceals, covers up, falsifies, or makes a false entry in any record, document, or tangible object with the intent to impede, obstruct, or influence the investigation or proper administration of any matter within the jurisdiction of any department or agency of the United States or any case filed under title 11, or in relation to or contemplation of any such matter or case, shall be fined under this title, imprisoned not more than 20 years, or both.*

New 18 U.S.C. § 1520 provides:
(a)(1) Any accountant who conducts an audit of an issuer of securities to which section 10A(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78j-l(a)) applies, shall maintain all audit or review workpapers for a period of 5 years from the end of the fiscal period in which the audit or review was concluded.

(2) The Securities and Exchange Commission shall promulgate, within 180 days, after adequate notice and an opportunity for comment, such rules and regulations, as are reasonably necessary, relating to the retention of relevant records such as workpapers, documents that form the basis of an audit or review, memoranda, correspondence, communications, other documents, and records (including electronic records) which are created, sent, or received in connection with an audit or review and contain conclusions, opinions, analyses, or financial data relating to such an audit or review, which is conducted by any accountant who conducts an audit of an issuer of securities to which section 10A(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78j-l(a)) applies . . . .

(b) Whoever knowingly and willfully violates subsection (a)(1), or any rule or regulation promulgated by the Securities and Exchange Commission under subsection (a)(2), shall be fined under this title, imprisoned not more than 10 years, or both.

(c) Nothing in this section shall be deemed to diminish or relieve any person of any other duty or obligation imposed by Federal or State law or regulation to maintain, or refrain from destroying, any document.

Sec. 805. Review of Federal Sentencing Guidelines for Obstruction of Justice and Extensive Criminal Fraud

Previous Law: Questions have arisen whether the Sentencing Guidelines sufficiently address obstruction of justice crimes.

Amendment: This section directs the Sentencing Commission to undertake an expedited review of these issues, particularly in light of the two new obstruction of justice statutes, described above. It also directs the Sentencing Commission to consider a number of factors such as destruction of a large amount of evidence, participation of a large number of individuals, or destruction of particularly probative or essential evidence, which might be considered sufficiently aggravating as to warrant additional enhancements or inclusion as offense characteristics. The Attorney General has advised the Sentencing Commission of this provision and asked the Commission to implement it fully and expeditiously.

Sec. 807. Criminal Penalties for Defrauding Shareholders of Publicly Traded Companies

Previous Law: Title 18 does not have a specific crime directly prohibiting securities fraud schemes. Prosecutors have found it necessary to reach many securities fraud schemes through the mail and wire fraud statutes. Securities fraud has also been prosecuted as a violation of provisions of title 15.
Amendment: New 18 U.S.C. § 1348 creates a specific felony for securities fraud punishable by up to 25 years incarceration. This provision complements existing securities law. The statute requires a nexus to certain types of securities, no proof of the use of the mails or wires is required. The text of the new section provides:

Whoever knowingly executes, or attempts to execute, a scheme or artifice-

(1) to defraud any person in connection with any security of an issuer with a class of securities registered under section 12 of the Securities Exchange Act of 1934 (15 U.S.C. 781) or that is required to file reports under section 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 780(d)); or

(2) to obtain, by means of false or fraudulent pretenses, representations, or promises, any money or property in connection with the purchase or sale of any security of an issuer with a class of securities registered under section 12 of the Securities Exchange Act of 1934 (15 U.S.C. 781) or that is required to file reports under section 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 780(d));

shall be fined under this title, or imprisoned not more than 25 years, or both.

Sec. 902. Attempts and Conspiracies to Commit Criminal Fraud Offenses

Previous Law: Under Chapter 63 (Mail Fraud) of Title 18, conspiracies to violate the mail fraud statute (§ 1341), the wire fraud statute (§ 1343), the bank fraud statute (§ 1344) and the health care fraud statute (§ 1347) are punishable by a maximum 5 year sentence. The wire fraud offense did not explicitly reach "attempts" to commit the substantive offense. However, this was not an impediment in practice, because proof of a scheme to defraud did not necessarily require proof that the scheme was successful.

Amendment: New 18 U.S.C. § 1349 provides that attempts and conspiracies to commit the substantive Federal fraud offenses listed above, as well as the new securities fraud offense, will have the same maximum punishment as the substantive crime. This section also effectively adds an "attempt" to commit the wire fraud offense as a federal crime. The remainder of the fraud statutes listed above already include "attempts."

New 18 U.S.C. § 1349 provides:

Any person who attempts or conspires to commit any offense under this chapter shall be subject to the same penalties as those prescribed for the offense, the commission of which was the object of the attempt or conspiracy.

Sec. 903. Criminal Penalties for Mail and Wire Fraud

Previous Law: The maximum term of imprisonment for violations of the mail and wire fraud statutes (18 U.S.C. §§ 1341, 1343) is 5 years, with the exception of fraud affecting a financial institution, which has a maximum term of incarceration of up to 30 years.
Amendment: This section amends 18 U.S.C. §§ 1341 and 1343 by increasing the maximum 5 year penalty for mail or wire fraud to 20 years. The maximum term of incarceration for fraud affecting a financial institution remains at a maximum of 30 years.

Sec. 904. Criminal Penalties for Violations of the Employee Retirement Income Security Act of 1974

Previous Law: Under 29 U.S.C. § 1131, any person who willfully violates the reporting and disclosure requirements concerning employee benefit plans as set forth in 29 U.S.C. §§ 1021-1031, or any regulation or order issued thereunder, is punishable by a fine, and/or a term of imprisonment not to exceed 1 year.

Amendment: This amendment increases the fines in Section 1131 to $100,000 (for an individual person), $500,000 (for persons other than an individual). Section 1131 also increases the maximum term of imprisonment from 1 year (a misdemeanor) to a maximum term of imprisonment of 10 years. The increase in the fine for individuals will have no limiting effect insofar as individuals convicted of violating Section 1131 will now be subject to the alternative fine provisions of 18 U.S.C. § 3571 for felony convictions. In the absence of restrictive language in Section 904 of the Act, individuals will be subject to the maximum fine of $250,000, or fine based on the defendant's gain or the victims loss, under § 3571. While the amendment also increases the fine in § 1131 to $500,000 for persons other than an individual, this change has merely increased the fine to the level of the maximum fine for an organization already set forth in § 3571.

Section 905. Amendment to the Sentencing Guidelines Relating to Certain White Collar Offenses

Previous Law: Questions have arisen whether the Sentencing Guidelines sufficiently address white collar offenses.

Amendment: This Section reaches beyond Section 803 of this Act, which addresses sentencing guidelines solely for obstruction of justice, to require that the Sentencing Commission study the existing guidelines and consider expedited issuance of amended guidelines within 180 days after enactment of this Act, which would address all the new criminal provisions and increased criminal penalties in this Act. This section also requires the Sentencing Commission to consider the broader issues of whether the white collar crime guidelines provide for sufficient deterrence and punishment, and assure reasonable consistency with other relevant directives and guidelines. The Attorney General has advised the Sentencing Commission of this provision and asked the Commission to implement it fully and expeditiously.

Section 906. Corporate Responsibility for Financial Reports

Previous Law: There are no statutory requirements that the chief executive officer or the chief financial officer certify certain periodic corporate financial statements. By instructions issued by the SEC for periodic and other filings, there was a general requirement that the forms had to be signed by officers, and in the case of annual reports, by a majority of the directors as well. These signing requirements did not include any type of certification or other attestation regarding the accuracy or completeness of the report. On June 20, 2002, the SEC published a
Notice of Proposed Rulemaking, contemplating a requirement that a company's chief executive officer and chief financial officer certify that the information contained in its financial reports is complete and true in all important respects. See 67 Fed. Reg. 41877 (2002). More recently, the SEC issued an order requiring that the principal executive officer and principal financial officer of the largest 947 companies whose securities are registered with the SEC certify the completeness, truth and accuracy of the most recent annual report, subsequent 10-Q and 8-K reports, and proxy materials filed with the Commission.

**Amendment:** This section enacts new 18 U.S.C. § 1350, which creates a requirement that the chief executive officer and the chief financial officer (or the equivalent thereof) of the "issuer" provide a statement which certifies that the periodic reports containing the financial statements, filed by an issuer with the SEC, fully comply with the requirements of Sections 13(a) and 15(d) of the Securities Exchange Act of 1934, and that the information contained in the periodic reports fairly presents, in all material respects, the financial condition and results of operations of the issuer. Certifying a report, knowing that it does not comport with all of the requirements of § 1350, is punishable by a fine of not more than $1,000,000 and imprisonment of up to 10 years. A willful violation is punishable by a fine of not more than $5,000,000 and imprisonment of up to 20 years.

New Section 1350 provides:

(a) CERTIFICATION OF PERIODIC FINANCIAL REPORTS.- Each periodic report containing financial statements filed by an issuer with the Securities Exchange Commission pursuant to section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m(a) or 78o(d)) shall be accompanied by a written statement by the chief executive officer and chief financial officer (or equivalent thereof) of the issuer.

(b) CONTENT.- The statement required under subsection (a) shall certify that the periodic report containing the financial statements fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)) and that information contained in the periodic report fairly presents, in all material respects, the financial condition and results of operations of the issuer.

(c) CRIMINAL PENALTIES.- Whoever

(1) certifies any statement as set forth in subsections (a) and (b) of this section knowing that the periodic report accompanying the statement does not comport with all the requirements set forth in this section shall be fined not more than $1,000,000 or imprisoned not more than 10 years, or both; or

(2) willfully certifies any statement as set forth in subsections (a) and (b) of this section knowing that the periodic report accompanying the statement does not comport with all the requirements set forth in this section shall be fined not more than $5,000,000, or imprisoned not more than 20 years, or both.
Sec. 1102. Tampering with a Record or Otherwise Impeding an Official Proceeding.

Previous Law: Title 18 U.S.C. § 1512, in part, provides a 10 year maximum term of incarceration for an offender who corruptly persuades another person with the intent to, in part, destroy or alter evidence.

Amendment: The amendment adds new subsection (c) to Section 1512 and renumbers existing subsections (c) through (i) as (d) through (j). New subsection (c) imposes a fine and/or a term of imprisonment of up to 20 years on any person who corruptly alters, destroys, mutilates or conceals a record, document or other object with the intent to impair the object's integrity or availability for use in an official proceeding, or who corruptly otherwise obstructs, influences or impedes an official proceeding. Section 1512, as amended, should be read in conjunction with the new Section 1519, added by section 802 of this Act, which criminalizes certain acts intended to impede, obstruct or influence "any matter" within the jurisdiction of any Department or agency of the United States, or in relation to or contemplation of any such matter. The term "corruptly" shall be construed as requiring proof of a criminal state of mind on the part of the defendant.

New Section 1512 (c) provides:

(c) Whoever corruptly-

(1) alters, destroys, mutilates, or conceals a record, document, or other object, or attempts to do so, with the intent to impair the object's integrity or availability for use in an official proceeding; or

(2) otherwise obstructs, influences, or impedes any official proceeding, or attempts to do so,

shall be fined under this title or imprisoned not more than 20 years, or both.

Section 1104. Amendment to the Federal Sentencing Guidelines

Previous Law: Questions have arisen whether the current Sentencing Guidelines sufficiently address securities, accounting, and pension fraud, and related offenses.

Amendment: This section requests the Sentencing Commission to study existing guidelines and consider expedited issuance of amended guidelines within 180 days after enactment of this Act, which address securities, accounting, and pension fraud, and related offenses. The Attorney General has advised the Sentencing Commission of this provision and asked the Commission to implement it fully and expeditiously.

Section 1106. Increased Penalties Under Securities Exchange Act of 1934

Previous Law: Section 78ff of Title 15, Sec. 32(a) of the Securities Exchange Act of 1934, provides for a criminal fine of $1,000,000 for individuals and/or imprisonment of up to 10 years, or a fine of $2,500,000 for anyone other than an individual.
Amendment: This amendment increases the fine amounts to $5,000,000 and $25,000,000 respectively, and raises the maximum term of imprisonment to 20 years.

Section 1107. Retaliation Against Informants

Previous Law: There is no explicit protection from retaliation for an individual who provides truthful information to a law enforcement officer concerning the commission or possible commission of a Federal offense.

Amendment: New subsection (e) of 18 U.S.C. § 1513 creates a felony offense for any person knowingly to take any action, with intent to retaliate, harmful to a person who provides such information concerning a federal offense.

New subsection (e) of § 1513 provides:

(e) Whoever knowingly, with the intent to retaliate, takes any action harmful to any person, including interference with the lawful employment or livelihood of any person, for providing to a law enforcement officer any truthful information relating to the commission or possible commission of any Federal offense, shall be fined under this title or imprisoned not more than 10 years, or both.

Retroactive Application of the New Provisions:

The Ex Post Facto Clause prohibits, inter alia, punishing as a crime an act an act previously committed that was innocent when done and increasing the punishment for a crime after its commission. See, e.g., Carmell v. Texas, 520 U.S. 513, 522 (2000); Collins v. Youngblood, 497 U.S. 37, 42 (1990). The Act adds several new criminal provisions: 18 U.S.C. 1519 and 1520 (added by Section 802); 18 U.S.C. 1350 (added by Section 906); 18 U.S.C. 1512(c) (added by Section 1102), and 18 U.S.C. 1513(e) (added by Section 1107). Those new criminal provisions will apply only to criminal conduct committed after the effective date of the Act. The Act also includes criminal provisions increasing the punishment for some existing criminal offenses: 29 U.S.C. 1131 (added by Section 904) and 15 U.S.C. 78ff (added by Section 1106). The increased penalties set forth in those provisions will apply only to criminal conduct committed after the effective date of the Act.

Section 807 adds a new criminal provision, 18 U.S.C. 1348, that creates a felony for securities fraud punishable by up to 25 years' imprisonment. Section 903 amends the existing mail and wire fraud statutes, 18 U.S.C. 1341 and 1343, to increase the maximum term of imprisonment for schemes to defraud not affecting financial institutions to 20 years' imprisonment. Those provisions will apply to any criminal conduct committed after the effective date of the Act. It is unclear, however, whether those provisions can be applied to schemes to defraud that straddle the effective date of the Act, i.e., schemes begun before the effective date of the Act but continuing after the effective date of the Act. Generally, mail and wire fraud offenses are complete upon the use of the mails or wires. See, e.g., United States v. Barger, 178 F.3d 844, 847 (7th Cir. 1999). Similarly, the new securities fraud offense will likely be considered complete upon the execution of the scheme. Cf. United States v. De La Mata, 266 F.3d 1275, 1287 (11th Cir. 2001) (bank fraud statute, 18 U.S.C. 1344), cert. denied, 122 S. Ct.
1543 (2002). The Ex Post Facto Clause likely bars applying the new provisions to schemes to defraud that extend beyond the effective date of the Act if the use of the mails or wire in a mail or wire fraud scheme occurred before the effective date of the Act or the execution of a securities fraud scheme occurred before the effective date of the Act. On the other hand, the Ex Post Facto Clause should pose no bar to applying the new provisions to schemes to defraud that began before the effective date of the Act if the use of the mails or wire in a mail or wire fraud scheme occurred after the effective date of the Act or the execution of a securities fraud scheme occurred after the effective date of the Act.

Finally, Section 902 adds a new criminal provision, 18 U.S.C. 1349, that punishes attempts and conspiracies to commit fraud offenses, including the new securities fraud offense. The Ex Post Facto Clause should pose no bar to applying that provision to a conspiracy that straddles the effective date of the Act because conspiracy is considered a continuing offense. See, e.g., United States v. Hersh, No. 00-14592, 2002 WL 1574990 (11th Cir. July 17, 2002).
Statement by the President

Today I have signed into law H.R. 3763, "An Act to protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws, and for other purposes." The Act adopts tough new provisions to deter and punish corporate and accounting fraud and corruption, ensure justice for wrongdoers, and protect the interests of workers and shareholders.

Several provisions of the Act require careful construction by the executive branch as it faithfully executes the Act.

The legislative purpose of sections 302, 401, and 906 of the Act, relating to certification and accuracy of reports, is to strengthen the existing corporate reporting system under section 13(a) and 15(d) of the Securities Exchange Act of 1934. Accordingly, the executive branch shall construe this Act as not affecting the authority relating to national security set forth in section 13(b) of the Securities Exchange Act of 1934.

To ensure that no infringement on the constitutional right to petition the Government for redress of grievances occurs in the enforcement of section 1512(c) of title 18 of the U.S. Code, enacted by section 1102 of the Act, which among other things prohibits corruptly influencing any official proceeding, the executive branch shall construe the term "corruptly" in section 1512(c)(2) as requiring proof of a criminal state of mind on the part of the defendant.

Given that the legislative purpose of section 1514A of title 18 of the U.S. Code, enacted by section 806 of the Act, is to protect against company retaliation for lawful cooperation with investigations and not to define the scope of investigative authority or to grant new investigative authority, the executive branch shall construe section 1514A(a)(1)(B) as referring to investigations authorized by the rules of the Senate or the House of Representatives and conducted for a proper legislative purpose.

GEORGE W. BUSH
THE WHITE HOUSE,
July 30, 2002.
TO: [DOCUMENT CUSTODIAN]

FROM: [ ]
Office of the General Counsel

RE: Document Review Responsibilities

DATE: xxxxxxx

You have agreed to act as corporate document custodian for the limited purpose of [Company’s] response to a subpoena (“Subpoena”) from a Grand Jury of the United States District Court for the District of Columbia (“Grand Jury”). The categories of documents requested and the memorandum I have sent to various employees, are attached.

Your responsibilities are as follows:

1. Supervise the collection of documents responsive to the Subpoena.

2. Follow up with those employees believed to have responsive documents to assure compliance.

3. Obtain certifications from such employees of their search and forwarding of responsive documents.

4. Forward such responsive documents to the company’s attorneys for submission to the government.

If you have any questions regarding these matters, please contact me or our outside counsel representing us in this matter.
Privileged and Confidential

[Date]

To: [ ] Employees

From: [In-House General Counsel]

Re: Document Retention Notice

As you may know, individual plaintiffs purporting to represent the Company’s public shareholders recently filed several class action lawsuits against the Company and certain of its officers. The Company strongly denies the charges contained in these lawsuits and intends to vigorously defend itself and its officers against these charges.

At some point in this litigation, the Company may be called upon to produce various documents to the plaintiffs. Accordingly, it is critical that the you take immediate steps to prevent the loss or destruction of any documents in the Company’s possession that relate to the events described in the lawsuits. Moreover, new Federal laws may make the actual or attempted destruction, alteration, mutilation, or concealment of relevant documents a criminal offense. The attached Schedule A contains a list of the general categories of documents that must be retained.

**Applicable Time Period.** Unless otherwise noted, this document retention notice applies to documents created or used during the period from [Date] through today.
Definition of “Documents.” Please note that the term "document," as used herein should be broadly construed to include not only conventional documents, but virtually any item that stores or communicates information. Thus, for example, you should retain (and prevent the destruction of) any computers, Palm Pilots, recordings, computer diskettes, CD-ROMs, brochures, photographs, magnetic tapes, or similar items that contain, in whole or in part, data relating to the categories of information set forth in Schedule A. Please also note that the term documents includes drafts, handwritten notes, e-mail printouts, message slips, sales slips, etc.

Your Questions. If you have any question about whether a specific document falls within the scope of this notice, or if you have any other questions or concerns regarding this notice, please contact __________ at __________.
SCHEDULE A

1. All documents relating to the Company’s communications with the investment community (e.g., shareholders, analysts, media, etc.), including all press releases, news articles, SEC filings, analysts’ reports, conference-call transcripts, etc.

2. All documents relating to the Company’s May 2001 agreement with [X Corporation] regarding the marketing and distribution of [product #1]. This category applies to all documents created or used during the period from January 2001 through today.

3. All documents relating to the Company’s marketing of [product #1] pursuant to the Company’s May 2001 agreement with [X Corporation]. This category applies to all documents created or used during the period from January 2001 through today.

4. All documents relating to the Company’s October 2000 agreement with [Y Corporation] regarding the marketing and distribution of [product #2]. This category applies to all documents created or used during the period from October 2000 through today.

5. All documents relating to the Company’s marketing of [product #2] pursuant to the Company’s October 2000 agreement with [Y Corporation]. This category applies to all documents created or used during the period from October 2000 through today.

6. All documents relating to [Z Corporation] efforts to market a form of [product #2]. This category applies to all documents created or used during the period from October 2000 through today.

7. All documents relating to the Company’s revenues and earnings projections
8. for the (i) third and fourth quarters of fiscal 2001; and (ii) fiscal years 2001 and 2002.
As you may know, the Company has recently been named in several shareholder suits. At some point in the process of the Company defending itself, it may be called upon to produce various documents to the plaintiffs. Moreover, new Federal laws may make the actual or attempted destruction, alteration, mutilation, or concealment of relevant documents a criminal offense. Accordingly, it is critical that you take appropriate steps to prevent the loss or destruction of any documents in the Company’s possession and with which you come into contact that may relate to the events described in the lawsuits. The attached Schedule A contains a list of the general categories of documents that must be retained.

**Definition of “Documents.”** Please note that, as used herein, the term "document" should be broadly construed to include not only conventional documents, but virtually any item that stores or communicates information. Thus, for example, you should retain (and prevent the destruction of) any computers, Palm Pilots, recordings, computer diskettes, CD-ROMs, brochures, photographs, magnetic tapes, or similar items that contain, in whole or in part, data relating to the categories of information set forth in Schedule A. Please also note that the term documents includes drafts, handwritten notes, e-mail printouts, message slips, sales slips, etc.

**Your Questions.** If you have any question about whether a specific document falls within the scope of this notice, or if you have any other questions or concerns regarding this notice, please contact [Name], at [phone number].
9. All documents relating to [    ], including any securities transactions relating to [    ].

10. All documents relating to any government investigation of the subjects identified in Item One.

3. All documents relating to any trading in [              ] securities.
Enclosed as attachment 1 are the categories of documents and records requested in a new subpoena (“Subpoena”) recently served upon [Company] by a Grand Jury of the United States District court for the District of Columbia. In an effort to respond to this Subpoena in the most sensible and efficient manner, we are directing the requests only to those employees who may have documents responsive to the requests. After each request set forth in Exhibit 1, we have indicated which employees are being asked to respond to the request. If there are employees in your organization whom you believe may have documents responsive to the request, but who are not listed after the request, please bring this to the attention of [Document Custodian], and he will see to it that they are also asked to search for responsive documents.

You should deliver the originals and existing copies of all documents sought by the Subpoena to [Document Custodian] in the legal office in [ ] as they are found and determined to fall within the scope of the subpoena. If there is any doubt about whether any item or object or document is sought by the Subpoena, it should be provided as part of the collection process. E-mail and saved files should also be searched for responsive data. You should be careful not to destroy or discard any documents sought by the Subpoena. All responsive documents should be delivered no later than ____ on ___________. If, for any reason, you cannot respond by or before that time, [Document Custodian] should be notified.

Employees who spend time collecting or reviewing documents sought by the Subpoena should charge their time to [time charge]

In order to demonstrate full compliance with the Subpoena, it is important that we be able to document fully the collection process. You should keep a written record of the search technique utilized. After the searches have been completed, the Certification included as Attachment 2 should be signed and sent to [Document Custodian].
The documents forwarded to [Document Custodian] will be returned to you. However, if you anticipate that you may need the document, or information from the document, in the near future, a copy of the document should be made for you to retain before the original is submitted. Please be certain that all non-identical copies (i.e., those with notations, etc) of the same document are produced.

Please note that negative responses are required on the attached certification form if no documents are located.

If you have any questions regarding the scope of the Subpoena or the instruction in this memorandum, please contact me as soon as possible.

cc: [Document Custodian]
Attachment 1

CATEGORIES OF DOCUMENTS SOUGHT BY THE GRAND JURY

• 1.
CERTIFICATION

I have received the memorandum from [Office of the General Counsel] dated xxxxxxx, which seeks documents responsive to the Subpoena from the Grand Jury of the United States District Court for the District of Columbia. I have reviewed all files within my possession, custody or control, and hereby state that

__________  I have found no responsive documents.

__________  I am forwarding all responsive documents with this certification.

__________  I have previously forwarded all responsive documents.

__________  I have previously forwarded some responsive documents and am attaching additional documents.

__________________________________________  ______________________
(Date)                                     (Signature)

__________________________________________  ______________________
(Print Name)

__________________________________________  ______________________
(Location)

__________________________________________  ______________________
(Telephone Number)

Return to: [Document Custodian]
MEMORANDUM TO EMPLOYEES

TO: Employees
FROM: [Manager]

We have recently been informed that the Inspector General of the U.S. Department of [______________] has begun an investigation into [______________]. The Company is cooperating and hopes that this matter can be cleared up as soon as possible.

The investigators asked for the names of Company employees who worked on these contracts, and we have given them those names. It is possible that [______________] investigator may telephone you or simply appear at your home to seek to interview you.

You should be aware of the law regarding such interviews:

- You have the right to decide whether or not you want to be interviewed.
- You have the right to have the interview conducted at a time and place of your own choosing.
- You may request that the interview be conducted only in the presence of a personal attorney or the Company’s counsel.
- You have the right to discontinue the interview at any time, especially if you believe you are being treated improperly or in an abusive manner.
- Any answers you give the investigators must be truthful.
- Any statement you make at the interview may be used against you and the company.
- You have the right to request a copy of the investigator’s notes.
• If you receive a written subpoena compelling you to testify, you must and should appear at the time, place and date set forth in the subpoena. Should that occur, please notify corporate counsel immediately.

All of these rights are your rights, and it is up to you whether or not to exercise them.

[If you wish to have an attorney available to you, the Company will consider paying reasonable legal fees associated with retaining that attorney up to a certain limit. In order to assist you, we have already arranged for a local attorney to be available to answer your questions. The local attorney with whom we have arranged for such consultations is [___________], and he/she can be reached at [telephone number]. It will be up to you whether or not that attorney represents you. If you wish to speak with that attorney to find out what he/she recommends you do, the attorney will not be conveying your views or questions to the Company or its counsel unless you are willing to have such information conveyed to us or to our lawyers. You should therefore feel free to contact this attorney to seek further details about what may happen as part of this investigation.

We are not writing you this letter to alarm you about the prospects of being interviewed. We anticipate that, by giving the government our full cooperation, this investigation will be concluded quickly and reasonably.

If you have any questions, please call me at [telephone number].

239726
My name is ________________________. As you may be aware, the Inspector General of the ______________________________ Department of is investigating the activities of the Company in __________________. We represent the Company and are conducting our own review and investigation of this matter. The Company has requested that all of its employees cooperate fully and completely in our efforts, and we trust that you will be forthcoming and truthful in your responses.

Although we do not represent you personally, what you tell us today is privileged from disclosure outside the Company. However, the Company may determine, in its own discretion, to advise government agencies and investigators, or others outside the Company, of the results of our work. The decision of whether to disclose this information will be made solely by the Company. If you believe it is necessary, you are free to retain your own lawyer. Should you need to retain an attorney, the Company, under appropriate circumstances and limits, may be prepared to advance you reasonable legal fees and costs and may recommend a lawyer.

Do you understand this?