Federal Monitors: What to Expect and How to Avoid Problems

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Panelists

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  - Former probation officer
  - Former federal prosecutor
  - Compliance expert
  - Federal Monitor for the “Girls Gone Wild” obscenity case

- Pam Johnston
  - Former federal prosecutor
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Core Question Today: Are Corporate Monitors Dragons or Sleuths?

Topics for Discussion

- History behind Monitors
- Nuts and Bolts of Monitorships
- A Monitor’s viewpoint
- Controversy surrounding Monitors and resulting reactions
- Take-aways
History of Monitors

History behind the Employ of Monitors

To understand the history, need to run through a few basic concepts –

- Prosecution of corporations and resolution of cases through deferred prosecution agreements and non-prosecution agreements
- Monitoring for compliance with the applicable laws during the period of the DPA or NPA
- Use of a monitor in place of a probation officer to “monitor” for such compliance
Increased prosecution of corporations – started around 2001

- Following the Enron scandal and others like it in the early 2000s, prosecutors initiated criminal investigations and enforcement actions against corporations with greater frequency

- To determine whether to prosecute corporations, prosecutors look to a number of factors

Factors relevant to DOJ when investigating corporations

- Nature and seriousness of the offense
- Pervasiveness of wrongdoing within the corporation
- Corporation’s history of similar conduct
- Corporation’s timely and voluntary disclosure of wrongdoing and its cooperation with the investigation
- Remedial actions taken by the corporation, including disciplining wrongdoers
- **Existence and adequacy of the corporation’s pre-existing compliance program**
- Collateral consequences to shareholders, pension holders, and non-culpable employees and impact on public arising from prosecution
- Adequacy of individual prosecutions or remedies such as civil or regulatory enforcement actions
Rise of the Deferred Prosecution and Nonprosecution Agreements

- Rise of the “Deferred Prosecution Agreement and the “Nonprosecution Agreement” – needed a tool that was less drastic than full blown prosecution
- Trying to prevent permanent injury to innocent third parties, including employees, pensioners, shareholders, creditors, customers, and the general public

Deferred Prosecution and Nonprosecution Agreements

- Under deferred prosecution and nonprosecution agreements, prosecutors agree to forestall prosecution in exchange for the corporation’s commitment to specific conditions set forth by the government
- Deferred prosecution agreements generally include a formal charging document (an “Information”) and must be approved by the court, while nonprosecution agreements typically do not include a charging document and are generally maintained by the parties
Deferred Prosecution and Nonprosecution Agreements

A deferred prosecution or a nonprosecution agreement may require the following:

- The implementation of a compliance program
- The waiver of corporate privileges (after protest, waiver has been used only in limited cases raising legitimate need)
- An admission of wrongdoing
- Stopping of certain activities
- The payment of fines and/or restitution
- The imposition of conditions unrelated to the investigation
- A “Monitor” who will oversee the corporation during the DPA/NPA

Deferred Prosecution and Nonprosecution Agreements

- Prosecutors have the upper hand in negotiations – many terms are set in stone
- The requirement of a “monitor” however is not one of the terms set in stone – it is negotiable
- The prosecutor may reserve the right to unilaterally declare a breach of the agreement and thereafter prosecute the corporation
- The court may reject a deferred prosecution agreement if it determines that the agreement is contrary to the U.S. Sentencing Guidelines
Compliance programs – complying with the U.S. Sentencing Guidelines

To be considered an “effective” compliance program under the U.S. Sentencing Guidelines requires the following:

• The organization must establish standards and procedures to prevent and detect criminal conduct
• The organization’s governing authority must be knowledgeable about the content and operation of the compliance and ethics program and must exercise reasonable oversight with respect to the implementation and effectiveness of the compliance program
• The organization should not include within the substantial authority personnel of the organization any individual that has engaged in illegal activities or other conduct inconsistent with an effective compliance program
• The organization must take reasonable steps to communicate periodically and in a practical manner its standards and procedures to high-level personnel, substantial authority personnel, as well as the organization’s employees and agents
• The organization must take reasonable steps
  • To ensure that the organization’s compliance program is followed, including monitoring and auditing to detect criminal conduct
  • To evaluate periodically the effectiveness of the organization’s compliance program
  • To have and publicize a system, which may include mechanisms that allow for anonymity or confidentiality, whereby the organization’s employees and agents may report or seek guidance regarding potential or actual criminal conduct without fear of retaliation

Compliance – Complying with the US Sentencing Guidelines

• The compliance program must be promoted and enforced consistently throughout the organization through:
  • Appropriate incentives to perform in accordance with the compliance program
  • Appropriate disciplinary measures for engaging in criminal conduct and for failing to take reasonable steps to prevent or detect criminal conduct
• After criminal conduct has been detected, the organization must take reasonable steps to respond appropriately to the criminal conduct and to prevent further similar criminal conduct, including making any necessary modifications to the organization’s compliance program
Why Prosecutors Employ and Corporations Agree to Monitors

- Prosecutors can’t do it – no time or interest
- No probation officer able to do it – no sentence
- Companies want to avoid criminal convictions
- Monitors grant prosecutors greater ability to ensure that change is implemented
- Agreements requiring monitors allow flexibility to achieve unrelated goals, which can serve as positive PR for the corporation

Nuts & Bolts of Monitors
Are Corporate Monitors: Dragons or Sleuths?

Answer: Both

Nuts & Bolts: Role of Monitors

- Monitors serve as informal, non-governmental corporate probation officers

- A monitor is an independent third party, generally an attorney or an accountant, tasked with ensuring that a corporation complies with a DPA or NPA
Nuts & Bolts: Frequency – 60%

- Monitors have been used in a variety of cases, including tax violations, Foreign Corrupt Practices Act violations, obscenity, securities fraud, environmental violations, health care fraud, and medical device off-label marketing
- Between 2003 and 2007, monitors were used in 60% of deferred prosecution and nonprosecution agreements (disclosed in the 35 reported agreements entered into during that period)

Nuts & Bolts: Reporting and Powers

- Monitors typically report to DOJ rather than to the court
- Most monitors’ reports are not made public
- Monitors are sometimes given sweeping oversight powers and the authority to make recommendations or decisions regarding corporate governance for a specified period of time
- Monitors do become involved in matters unrelated to the agreements (e.g., Pharma monitor recommended the CEO’s dismissal after an unrelated criminal patent dispute)
Nuts & Bolts: Duration

- During the term of the DPA or NPA
- The length of monitoring varies, but, on average, lasts two years
- Some last as long as five years

A Monitor’s Viewpoint
A Monitor’s Viewpoint

- Compare it to being a probation officer
- Power – depending on the wording of the DPA
- The relationships
  - Govt
  - Court
  - Defense counsel
  - Company personnel

A Monitor’s Viewpoint

- Formal guidance (or lack thereof)
- Purpose
- Compliance
- Role of the reports
- Second chances
- Value of being open on close issues
- Scope of assignment
Comments Regarding The Monitorship of a Professional Firm

- An accounting firm was investigated for aiding and abetting tax evasion
- In 2004, DOJ filed a criminal complaint against the firm
- In August 2005, before an indictment had been issued, prosecution halted because DOJ, IRS, and the firm entered into a DPA

Contents of this Deferred Prosecution Agreement

- Required admission of wrongdoing
- Required payment of $456 million to the IRS
- Restricted the tax practice, such that the firm was not permitted to take on new private tax clients nor sell certain pre-packaged tax products
- Required permanent, continued cooperation with the DOJ
- Required the creation of a permanent compliance office and a permanent educational and training program relating to law and ethics
- Required the creation of a hotline for whistleblowers
- Permitted DOJ to appoint a monitor to serve for three years and review the firm’s compliance with the agreement
- Permitted the IRS also to monitor the tax practice for an additional two years after the monitor left
Example of the Monitor's Scope of Authority

- Review and monitor the firm's ethics program
- Given unrestricted access to information (e.g., access to correspondence or emails)
- Empowered to call a meeting or interview any partner, employee, or agent
- Given the authority to employ legal counsel, consultants, investigators, experts, and other personnel necessary to assist in discharge of monitor's duties
- Given authority to “take any other actions that are necessary to effectuate his or her oversight and monitoring responsibilities”
- To be paid by the firm

Unusual Terms of Agreements for Monitors to Oversee

- Bristol-Myers was required to fund the chair in ethics at Seton Hall Law School
- Operations Management International required to donate to the Coast Guard Alumni Association and fund a chair in environmental studies
- Roger Williams Medical Center required to provide $4 million in additional free uninsured health care to low-income residents
- New York Racing Association required to install slot machines at its race tracks
- MCI required to add 1600 new jobs over ten years in Oklahoma
Controversy and Resulting Reactions

Controversy Surrounding Monitors

- Some monitors received lucrative payouts (AG Ashcroft example—$27.52 M for 18 months work)
- Small company – can be done for $200-250k a year
- The monitor selection process is oftentimes unknown (corp not always given opportunity to object)
- The monitor’s identity is generally unavailable to the public
- Conflicts of interest can arise
- There were few guidelines for prosecutors to follow
New DOJ Guidelines Relating To Use of Monitors

- As of March 2008, there are now DOJ guidelines.
- Prosecutors are to notify the appropriate U.S. Attorney (“USA”) or Department Component Head (“DCH”) before signing an agreement requiring a monitor.
- The USA or DCH must provide a copy of the agreement to the Criminal Division Assistant Attorney General.

New DOJ Guidelines Relating To Use of Monitors

- The selection process must be designed to:
  - Select a highly qualified and respected person.
  - Avoid potential and actual conflicts of interest.
  - Instill public confidence.
- A monitor is an independent third-party, not an employee or agent of the corporation or of the Government.
New DOJ Guidelines Relating To Use of Monitors

- A monitor’s primary responsibility is to assess and monitor a corporation’s compliance with the terms of the agreement that are specifically designed to address and reduce the risk of recurrence of the corporation’s misconduct.
- A monitor’s responsibilities should be no broader than necessary to address and reduce the risk of recurrence of the corporation’s misconduct.

New DOJ Guidelines Relating To Use of Monitors

- Communication among the Government, the corporation, and the monitor is in the interest of all the parties.
- If a corporation chooses not to adopt recommendations made by the monitor within a reasonable time, either the monitor or the corporation should report that fact to the Government, along with the corporation’s reasons.
New DOJ Guidelines
Relating To Use of Monitors

- The agreement should clearly identify any type of previously undisclosed or new misconduct that the monitor will be required to report directly to the Government
- The duration of the agreement should be tailored to the problems that have been found to exist and the types of remedial measures needed for the monitor to satisfy their mandate
- In most cases, an agreement should provide for an extension of or the termination of the monitor provision at the discretion of the Government depending on the circumstances

July 2008 -- Proposed Legislation-H.R. 6492

- July 2008 – Sought to impose rules re monitors, DPAs, and NPAs – NEVER PASSED
- Main components:
  - Circumstances in which a monitor is warranted and the duties and authority of such a monitor
  - What terms and conditions are appropriate in the agreement
  - The process by which the DOJ determines that an organization has successfully satisfied the terms of the agreement, or has breached the agreement
  - Extent of joint involvement of regulatory agencies in connection with the agreement
  - Period during which the agreement should remain in effect
  - What constitutes cooperation, if any, required by the agreement from the organization and its employees with respect to any ongoing criminal investigations
  - When a prosecutor should enter into a nonprosecution agreement rather than a deferred prosecution agreement
Proposed Legislation-H.R. 6492

- Would impose rules for selecting monitors
  - Requires creation and publication of a national list of organizations and individuals who have expertise and specialized skills necessary to serve as monitors
  - Requires an open, public, and competitive process for the selection of a monitor, which must be approved by the court
  - Establishes a fee schedule for the compensation of monitors, which must be available to the public

Proposed Legislation-H.R. 6492

- Prohibits the payment of money to a third party other than the monitor or the monitor’s staff if the payment is unrelated to the harm caused by the wrongdoing
- Prohibits attorneys who are or might participate in the prosecution to have a role in the selection of the monitor
- Requires that the parties file quarterly reports on the progress made toward the completion of the agreement
**Take-Aways**

- Best to try to avoid in the first place
- Seek to implement a strong compliance program and culture
- Try to have objective internal systems
- Pay money to avoid a monitor
- Be proactive, if there’s a monitor
- Play it straight with the monitor

**Questions?**

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