

Who Guards the Guardian?

The Justice Department can monitor corporate monitors just fine.



BY JOSHUA R. HOCHBERG

On the heels of several lucrative appointments of former government officials to monitor corporations in connection with criminal settlement agreements, Congress is considering restricting the Justice Department's negotiation of these deferred and nonprosecution agreements and its selection of corporate monitors.

The proposed legislation is not the answer. The Justice Department possesses the expertise and the willingness to respond to public concerns, and it should be allowed to implement necessary reforms on its own.

The Accountability in Deferred Prosecution Act of 2008 (introduced on July 15, as H.R. 6492) seeks to regulate the Justice Department's use of deferred prosecution agreements and nonprosecution agreements to resolve corporate investigations. The act would require the Justice Department to issue written guidelines on the use of these agreements. It also legislates procedures for the selection and compensation of independent corporate monitors and requires that all such agreements be approved and supervised by a court.

If enacted, the act would make these agreements more transparent. But it would also intrude upon the discretion traditionally exercised by the Justice Department when it declines to bring formal criminal charges.

The act is also premature. The Justice Department has taken the threat of congressional action seriously in the past by reissuing internal guidelines and by sending letters to Congress promising reforms. Enacting this legislation would deprive the department of an opportunity to respond appropriately. It is thus both unwise and unnecessary.

DEFERRING PROSECUTION

Deferred prosecution agreements involve the filing of criminal charges that are held in abeyance during the term of the agreement. In contrast, nonprosecution agreements do not involve formal charges.

In the last several years, these agreements have grown from simple letter agreements of a few pages into formal 25-page contracts detailing cooperation and compliance efforts, with lengthy addendums defining the duties of corporate monitors and stating agreed-upon facts. The agreements are often accompanied by side letters and parallel civil settlements with the Securities and Exchange Commission.

In recent correspondence with Congress, the Justice Department identified 85 deferred and nonprosecution agreements used to settle corporate fraud cases, most of which have occurred since 2003. Approximately half of these resolutions required a third-party monitor. These cases have involved accounting and securities fraud, Foreign Corrupt Practices Act violations, money laundering, fraud in the Oil for Food program, and health and medical device investigations.

The Justice Department maintains that these agreements save resources and minimize litigation, decrease negative consequences for innocent parties, achieve restitution, aid in the prosecution of individual defendants, and require ethics and compliance programs by companies. The use of these agreements increased dramatically following the criticism of the department's prosecution of Arthur Andersen in 2002.

The momentum for the Accountability Act was generated by the September 2007 settlements between the U.S. attorney for the District of New Jersey and five companies representing 95 percent of the market in hip and knee surgical implants. In the settlements, the U.S. attorney selected several former U.S. attorneys and Justice Department officials as corporate monitors, the most prominent being former Attorney General John Ashcroft. Ashcroft was named as monitor of Zimmer Inc., and the company estimated that his fees could exceed \$50 million. The companies admitted no wrongdoing, a significant departure from most agreements.

THE MORFORD MEMO

In March 2008, on the eve of a congressional hearing on corporate monitor selection, the Justice Department issued the

memorandum “Selection and Use of Monitors in Deferred Prosecution Agreements and Non-Prosecution Agreements with Corporations” (known as the Morford memo after its author, Craig Morford, then acting deputy attorney general), which provides principles to guide prosecutors in drafting provisions on the use of monitors.

Significantly, the Morford memo requires that both the Office of the Deputy Attorney General and an ad hoc committee in the prosecutor’s office approve each monitor’s appointment, thereby ensuring review of potentially unilateral and political decisions by U.S. attorneys.

The Morford memo also provides that a monitor’s primary responsibility is to assess and oversee the corporation’s compliance with those terms of the agreement specifically designed to address the risk of misconduct recurring. This may include reporting new misconduct to the Justice Department. Investigation of historical misconduct is not encouraged, however, unless it would help inform the monitor’s evaluation of the company’s compliance.

A NEW LAW?

The Accountability Act requires the Justice Department to establish guidelines on the appropriate terms and conditions for deferred and nonprosecution agreements, which go well beyond the criteria for selection of monitors.

These guidelines would be required to address when and whether monetary penalties and restitution are appropriate, the process for determining either satisfaction or breach of the terms of the agreements, the extent of joint involvement of regulatory agencies, the appropriate time period for the agreements, what constitutes cooperation by the entity with ongoing criminal investigations, and whether a nonprosecution agreement rather than a deferred prosecution agreement is appropriate.

The act requires that all deferred and nonprosecution agreements be filed in federal district court for a judicial determination of whether the agreement is consistent with the Justice Department guidelines and in the interests of justice. The court would also be required under the act to oversee the progress made toward completion of the agreement through reports submitted on a quarterly basis by the parties and the monitor.

Notwithstanding the reforms in the Morford memo, the Accountability Act sets forth specific requirements for the selection and compensation of corporate monitors. The Justice Department is directed to establish rules for the selection of monitors and to create a national list of organizations and individuals who have the necessary expertise and specialized skills. This competitive process for the selection of each monitor is ultimately subject to court approval. The Justice Department must also establish a public fee schedule for the compensation of monitors.

AN UNWORKABLE CONCEPT

The Accountability Act undoubtedly makes the imposition of deferred and nonprosecution agreements more transparent. Along the way to that laudable goal, however, it effectively does away with nonprosecution agreements, establishes a costly and time-consuming procedure requiring that all settlements

receive court approval, and promotes an unworkable concept of approved monitors and fees.

Congress can achieve its goal of greater transparency simply by requiring periodic reports from the Justice Department that disclose all negotiated settlements and the use of monitors in those settlements.

Requiring court approval of a nonprosecution agreement means the end of such agreements. Even if the court has jurisdiction, companies that prefer such agreements will realize that a court-filed nonprosecution agreement is really no different than the deferred prosecution agreements already filed with the court.

The Morford memo already addresses the selection process for monitors and calls for a pool of at least three qualified candidates from which the company will choose each monitor. The act’s proposals concerning monitor selection do little to improve on this process.

In particular, the qualifications, expertise, and costs of the monitor will vary widely depending on the case. Many qualified monitors may be suitable only for certain types of matters. Others will be reluctant to put their name on a pre-qualified list because of the potential conflicts this could create for current clients under investigation. The selection process thus needs to include consideration of the nature and location of the work, the expertise and resources that will be needed, and the monitor’s role and budget.

TIME FOR DETAILS

The Justice Department needs time to demonstrate the efficacy of the Morford memo and to consider additional guidance. The department should try to pre-empt the legislation and consider more explicit guidance to rein in individual offices and standardize the nationwide handling of corporate settlements.

In particular, model deferred and nonprosecution agreements would be useful. Monitors should be required to submit budgets and work plans as part of the selection process, and these should be reviewed and modified before selection.

The department also needs to provide guidance on a multitude of details. When can agreements be used in conjunction with guilty pleas? Are side agreements with parent companies appropriate, and which corporate entity should be sanctioned? Should monitors ever have the power to do anything other than make recommendations and report? Should the “voluntary” disclosure of new wrongdoing be a monitor duty? If so, what corporate activity should be covered? Can a company pre-empt a monitor by hiring respected compliance experts? Do settlements with other agencies, such as entering an SEC consent decree or a corporate integrity agreement with the inspector general of Health and Human Services, negate the need for a monitor?

The Justice Department is better equipped than Congress to provide quick and effective guidance. Congress should allow the Justice Department time to respond to its concerns before pursuing intrusive legislation such as the Accountability Act.

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