White-Collar Criminal and Regulatory Enforcement: What You Need to Know Now

Wachtell, Lipton, Rosen & Katz

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Introduction

- **We now have a far clearer picture than we did last year of the white-collar and regulatory enforcement priorities of the Biden administration.**
- One-year+ into this administration, some themes are emerging:
  - Reaffirmation that **pursuing corporate criminal enforcement is a major priority;**
  - Signals of **more robust corporate regulatory enforcement from key agencies,** including the SEC, FTC, CFTC and EPA; and
  - **Stricter inquiries to earn cooperation credit in resolving corporate investigations**.
- We expect continued **aggressive enforcement in traditional priority areas**, such as FCPA, securities fraud, antitrust, anti-money laundering and sanctions.
- But we also see **significant new focus on less conventional areas**—*e.g.*, cyber breaches, cryptocurrencies, climate change and pandemic-related fraud.
- Enforcement in many areas is supported by regulatory initiatives and a more integrated approach across government departments and agencies.

Introduction *(Cont'd)*

- **The "talk" from the DOJ and SEC has been, in a word, "tough".**
  - AG Merrick Garland: "I have also seen the Justice Department's interest in prosecuting corporate crime wax and wane over time. Today it is waxing again."
  - DAG Lisa Monaco: "[W]e will **urge prosecutors to be bold in holding accountable those who commit criminal conduct"** and to "commence a case if [a prosecutor] believes that a putative defendant's conduct constitutes a federal offense, and that the admissible evidence will probably be sufficient to obtain and sustain a conviction."
  - DAG Monaco: "While the priority [in white-collar criminal enforcement] remains individual accountability, where appropriate, **we will not hesitate to hold companies accountable.**"
  - SEC Chair Gary Gensler: Invoking as timely today words from first SEC Chair Joseph Kennedy's first speech: "The Commission will **make war without quarter on any who sell securities by fraud or misrepresentation**." And emphasizing that the SEC will "use all of the tools in our toolkit to **investigate wrongdoing and hold bad actors accountable**…."
- **The administration has sought to back up the tough talk with concrete actions** that are important to understand when preparing for and responding to white-collar criminal and regulatory investigations.

DOJ Developments

- DOJ has made **three significant revisions to enforcement policies** that auger a return to a tougher, Obama-era approach to corporate criminal enforcement:
  - **Broadened Definition of Corporate Recidivism**: Prosecutors making charging decisions about a company must evaluate "all prior misconduct . . . when it comes to decisions about the proper resolution with a company, *whether or not that misconduct is similar to the conduct at issue in a particular investigation.*"
    - A company's "full criminal, civil and regulatory record" is relevant to corporate resolution decisions.
  - **Broadened Scope of Required Disclosures About Responsible Individuals**: Companies seeking cooperation credit will once again be required to provide the government with "*all* non-privileged information about individuals involved in or responsible for the misconduct at issue" regardless of position, status or seniority.
    - Companies cannot "limit disclosures to those *they* assess to be 'substantially involved'" in misconduct.
  - **Renewed Embrace of Corporate Monitorships**: Expressly "rescinding" prior DOJ guidance to the extent interpreted to "suggest[] that monitorships are disfavored or are the exception."
    - Monitors are appropriate when needed to ensure "a company is living up to its compliance and disclosure obligations under the DPA or NPA."

DOJ Developments *(Cont'd)*

- **Other DOJ policy pronouncements signal a tougher approach to corporate criminal enforcement:**
  - **Heightened focus on ensuring compliance with the terms of NPAs and DPAs**.
    - DAG Monaco: "We will hold accountable any company that breaches the terms of its DPA or NPA. **DPAs and NPAs are not a free pass**, and there will be serious consequences for violating their terms."
    - DOJ has notified two multinational companies of potential breaches of their respective DPA obligations because of each company's failure to timely share certain information concerning pre-DPA conduct and/or post-DPA conduct required to be disclosed under the respective DPAs.
  - **More probing assessment of "tone at the top," including that true cooperation in certain circumstances may require removal of top leadership, *even if not involved in the wrongdoing*.**
    - AAG Kenneth Polite: "[E]ven if there is not any evidence that a CEO personally committed a crime, upon discovery of a crime, a corporation should examine whether a change in leadership is necessary, not for change's sake, but because [the CEO] modeled poor ethical behavior for the workforce, or fostered a climate in which subordinates committed wrongdoing with intent to benefit the company, or permitted weak internal controls that allowed the crimes of individuals to go undetected."
  - **Evaluation of whether pre-trial diversion – *i.e.*, NPAs and DPAs – is appropriate for certain recidivist companies and whether other approaches can better "promote cultural and institutional changes that will have a greater impact on deterring misconduct."**

DOJ Developments *(Cont'd)*

- Additional signs of the DOJ's new, tougher stance:
  - Increasing funding and resources
    - FY 2022 budget includes funding to hire 120 additional prosecutors, on top of the 34 attorneys added to the DOJ's Criminal Fraud Section in FY 2021.
    - $325 million to hire 900 FBI agents to support the FBI's White-Collar Crime Program
  - Enhancing use of data analytics to identify potential wrong-doing and initiate cases.
    - Instead of simply relying on corporate self-reporting to generate cases.
  - Pursuing individual wrongdoers
    - This remains the DOJ's top priority in corporate criminal cases.
    - USAOs around the country charged 5,521 individuals with white-collar crimes in FY 2021 – representing a 10% increase over the prior year.
    - DOJ's Fraud Section charged 333 individuals in FY 2021, securing some 326 convictions by plea or trial verdict.

SEC Developments

- New SEC leadership has made clear it **intends to oversee a more aggressive regulatory and enforcement program**, and has taken concrete steps to do so.
- Priority areas include:
  - Accounting and Financial Reporting;
  - Insider Trading;
  - Cybersecurity and ESG/Climate-related Disclosure;
  - Crypto Assets; and
  - SPACs.
- As with DOJ, pursuing individual accountability is a top priority for the SEC.
  - SEC Chairman Gensler has pledged to **hold individuals accountable "without fear or favor**."
- SEC has expressly underscored its **expectations for earning cooperation credit**
  - Enforcement Director Grewal: The SEC Staff looks to "whether the would-be cooperator took significant, tangible steps that enhanced the quality of our investigation, allowed us to conserve resources and bring charges more quickly, or helped us to identify additional conduct or other violators that contributed to the wrongdoing."

SEC Developments *(Cont'd)*

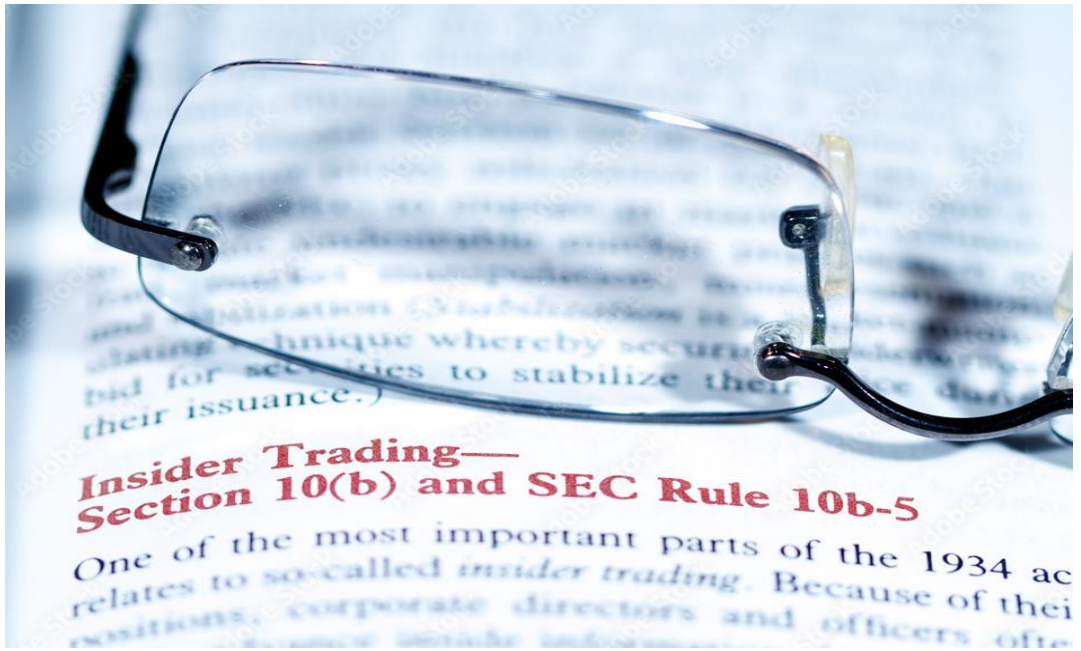
- **Requiring admissions in resolving enforcement cases**
  - The Enforcement Division has returned to a policy of requiring admissions of wrongdoing in selected settlements – an approach which projects a tougher image, but does not advance any identifiable policy goal.
- **Pursuing higher civil penalties in settlements**
  - The pendulum on penalty levels has swung back and forth over the years with changes in administrations.
  - Current Commission and Staff have said they intend to pursue higher civil penalties in connection with corporate settlements.
    - Statutory limits on penalty levels have not prevented the SEC in certain cases from seeking or obtaining penalty amounts in settlements that would be virtually impossible to obtain in litigation before a judge bound to apply the statutory criteria.
- **Continuing promotion of whistleblower program**
  - SEC announced in Fall 2021 it had passed the $1 billion milestone for awards under its whistleblower bounty program. Awards in 2021 alone totaled $564 million.
  - Current Commission and SEC Staff have taken steps to roll back earlier measures that they believe have undermined the program's effectiveness.

SEC Developments *(Cont'd)*

- **Accounting Fraud and Financial Reporting Cases are a Priority**
  - After a perceived downturn in investigative activity in recent years, the SEC has been pursuing more accounting fraud and financial disclosure cases.
- Examples Include the following **"no admit/no deny" settlements:**
  - Kraft Heinz Co. and two executives charged with expense management scheme ($62 million corporate penalty);
  - Baxter International and two executives charged with using improper intra-company FX transactions to misstate income ($18 million corporate penalty);
  - Healthcare Services Group and two executives charged with failing to accrue for and disclose material loss contingencies ($6 million corporate penalty);
  - American Renal Holdings and three executives charged with a "cookie jar" scheme involving revenue adjustments ($2 million corporate penalty); and
  - Ernst & Young and three partners charged with auditor independence violations ($10 million corporate penalty).

SEC Developments *(Cont'd)*

- Insider trading remains a major area of SEC enforcement focus.
- **Pursuit of Aggressive "Shadow Trading" Enforcement Theory** – an employee of a biopharmaceutical company who received information about the potential acquisition of his employer then traded in the securities of *another company* in the same small industry segment. This is a new enforcement theory, though still untested at the appellate court level.
- **Proposed new requirements for 10b5-1 plans to address SEC concerns about potential abuses:**
  - 120-day cooling-off period before first trade;
  - Certification of lack of awareness of material non-public information; and
  - Requirement that plan be entered into *and "operated"* in good faith (aimed at addressing the potential for manipulation in serial initiation and termination of plans by the same person).



SEC Developments *(Cont'd)*

- The **SEC has prioritized ESG issues**, cutting across multiple program areas.
- **Major ESG initiatives include**:
  - February 24, 2021 directive to the Division of Corporation Finance to **enhance scrutiny of climate-related disclosures in public company filings**.
    - The initiative resulted in a substantial number of comment letters directed to issuers.
  - March 4, 2021 formation of a **22-person Climate and ESG Task Force** within the Division of Enforcement.
    - The mission of the Task Force is to **proactively identify for investigation potential gaps or misstatements in issuers' disclosures of climate risks** and in investment adviser and fund statements about ESG investment strategies.
  - March 21, 2022 rulemaking proposal would **impose specific climate-related disclosure requirements**. If adopted, litigation over the SEC's authority to impose such rules is likely. The proposal would mandate disclosure of:
    - Oversight and governance in relation to climate-related issues;
    - Material risks and opportunities;
    - Data regarding greenhouse gas emissions;
    - Climate-related financial statement metrics; and
    - Information regarding a company's climate-related targets, goals and transition plans.

Cybersecurity Regulation and Enforcement

- **Growing importance of cybersecurity and disclosure** as risk areas for corporations.
  - White House 2021 Open Letter – cyberattacks threaten not just data security but core business operations.
- Enforcement responses to cyber incidents **increasingly extend beyond pursuit of cybercriminals and their backers** to focus instead on companies' detection of, response to, and disclosure of cyberattacks.
- **Three pillars of emerging enforcement** focus on targeted companies:
  - Pressure to adopt and disclose cybersecurity prevention, reporting and remediation protocols;
  - Pressure promptly to assess cyber incidents and report "material" breaches; and
  - Back-end enforcement.
- We have seen increased enforcement activity in this area.
  - *E.g.*, Fall 2021 DOJ Civil Cyber-Fraud Initiative – use of False Claims Act to pursue government contractors who fail to meet contractually required cybersecurity standards.
  - March 2022 – medical services provider failed to provide contracted-for secure medical records storage system. Initiative raises risk of *Qui Tam* cases focused on cybersecurity issues.

Cybersecurity Regulation and Enforcement *(Cont'd)*

- **Cyber Incident Reporting for Critical Infrastructure Act**
  - Signed into law in March 2022, but effective only upon issuance of implementing regulations
  - "Covered entities" appear defined very broadly – includes "communications," "critical manufacturing," "food and agriculture," and "healthcare," among other industries
  - Requires reporting of a "covered cyber incident" to CISA within 72 hours
  - Requires reporting of *any* ransomware payment within 24 hours
  - Government's intent is to harmonize CIRCIA requirements with other federal agency cyber incident reporting regimes
- **SEC's proposed cyber-related rules** for public companies
  - Would require 8-K disclosure within 4 business days of "material" cyber incident
  - Would amend Reg S-K to require recurring disclosures of cyber policies and procedures, including allocation of responsibility and oversight, and director expertise in cybersecurity
- Cyber-related developments **put a premium on robust internal detection systems and effective means of promptly flowing information** about incidents to levels at which materiality assessments and disclosure decisions can be made

Other Federal Enforcement Priorities

- **2021 FCPA enforcement statistics were significantly down from historical levels**
  - DOJ and SEC resolved three corporate FCPA investigations with total penalties of ~$160 million
  - DOJ and SEC resolved long-running Credit Suisse case involving foreign corruption but charged the company using non-FCPA statutes, with total penalties of ~$275 million
  - DOJ brought FCPA-related charges against eighteen individual defendants
- **But DOJ cautioned the business community to avoid becoming complacent in the wake of a downtick in FCPA enforcement statistics**
  - Reaffirmed that FCPA enforcement remains a significant priority
  - Media reports in 2021 noted the number of prosecutors in DOJ's FCPA unit at an all-time level
  - 2021 hire of attorney with substantial private sector compliance experience, including service on monitor team for DOJ's 2016 FCPA resolution with Brazilian petrochemicals firm Braskem
  - Significant number of still-open FCPA investigations
- **Current Administration has taken other important steps to set the stage for a coming era of aggressive FCPA enforcement**

Other Federal Enforcement Priorities *(Cont'd)*

- **June 2021 issuance of White House National Security Study Memorandum**
  - Declared the fight against foreign corruption a "core national security interest."
- **December 2021 issuance of U.S. Strategy on Countering Corruption**
  - Setting forth a "whole-of-government approach to elevating the fight against corruption."
  - Continued vigorous FCPA enforcement is a key element of the overall strategy.
- **FCPA Corporate Policy remains in place**
  - Presumption that DOJ will decline prosecution of a company that voluntarily discloses misconduct, cooperates proactively, implements timely and appropriate remedial steps, and disgorges any ill-gotten profits.
  - SEC may still pursue civil enforcement through books and records/internal accounting controls provisions of the FCPA.
  - Policy also provides opportunity for lower penalties even when DOJ initiates an investigation.
  - To date, DOJ has issued 15 declinations pursuant to its FCPA Corporate Enforcement Policy.
  - **Policy remains an important tool for companies to consider should potential issues arise.**

Other Federal Enforcement Priorities *(Cont'd)*

- **Use of economic sanctions increased significantly over the last 20 years**
  - U.S. maintains some two-dozen country-focused sanctions programs, ranging from total (or near total) embargoes to more targeted restrictions – latest example is expansive sanctions on Russia and related parties in response to Ukraine invasion.
- **October 2021 Department of Treasury Review of Sanctions Programs**
  - Reaffirmed importance of sanctions and related programs as important tools in service of national security, foreign policy, enforcement and other U.S. governmental interests.
  - Aim is to modernize approach to sanctions to ensure effectiveness in light of developments, such as digital assets, use of new payment systems and the rise of strategic economic competitors, which have led to new ways of hiding cross-border transactions and evading current sanctions.
- **DOJ Export Control and Sanctions Corporate Enforcement Policy**
  - Administered by DOJ's National Security Division Counterintelligence and Export Section
  - Modeled after FCPA Corporate Enforcement Policy – presumption of NPA and no fine; requires voluntary self-disclosure, full cooperation and timely and appropriate remediation.
- Companies operating internationally must have systems in place to **track relevant sanctions developments** and **timely update their compliance programs** accordingly.

Continuing Importance of State Attorneys General

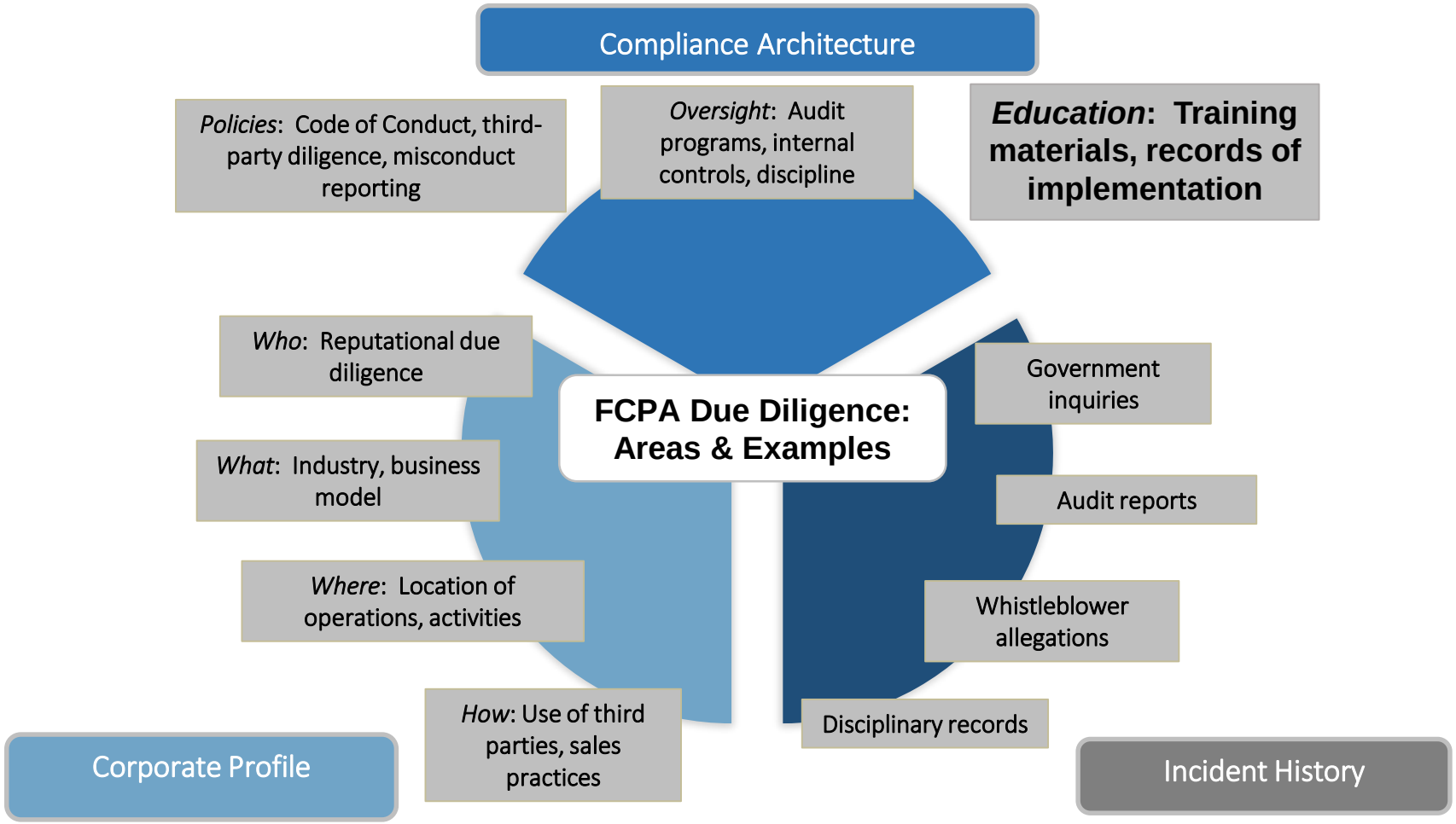
- **State AGs have been active in areas previously viewed as largely federal domains**: *e.g.*, antitrust; healthcare; environment; financial services and consumer protection.
  - **Antitrust** – varying coalitions of State AGs have brought a number of lawsuits against "Big Tech" companies seeking to challenge alleged anti-competitive conduct or past acquisitions. In September 2021, 32 AGs wrote to Congress in support of six bills that would strengthen the ability of State AGs to pursue antitrust actions.
  - **Opioids** – In a landmark settlement of lawsuits alleging drug manufacturers and distributors improperly marketed and distributed opioids, three drug distributors agreed to pay $21 billion, and one drug manufacturer $5 billion, to 46 and 45 states, respectively.
  - **Climate Change/Environment** – State AGs continue to pursue climate change actions against energy companies, despite setbacks in certain early cases – *e.g.*, in September 2021, 20 State AGs urged Congress to fund critical climate-change related programs, while some State AGs are creating dedicated environmental justice units.
  - **Workplace Conduct** – Six State AGs issued an April 6, 2022 letter to the NFL Commissioner stating their "grave concerns" about allegations that the NFL's workplace culture "is overtly hostile to women" and promising to "use the full weight of [their] authority to investigate and prosecute" such allegations.
- State AG investigations can be particularly burdensome -- *e.g.*, **simultaneous litigation in multiple jurisdictions; parallel federal/state investigations; and political considerations**.

Heightened DOJ Focus on Corporate Compliance Programs

- The DOJ Manual sets forth the factors prosecutors must consider in determining whether to bring criminal charges against a corporation, as well as in negotiating plea agreements, NPAs and DPAs.
  - These factors include **the adequacy and effectiveness of a corporation's compliance program at the time of the misconduct being investigated and at the time of a charging decision or pre-trial diversion**.
  - Evaluation of a **corporate compliance program is also critical in DOJ's consideration of whether to require a monitor in resolving a corporate criminal investigation**.
- AAG Polite, himself a former Fortune 500 Chief Compliance Officer, has stressed that **DOJ will conduct a searching review of corporate compliance programs** in making enforcement decisions.
  - DOJ has **greater compliance expertise and experience** than ever before.
  - **Substance matters** – An effective compliance program is **"much more than a company's policies, procedures, and internal controls**. We [DOJ] expect companies to implement compliance programs that: (1) are well designed, (2) are adequately resourced and empowered to function effectively, and (3) work in practice."
  - DOJ's message to corporate America – "[DOJ] want[s] to know whether you are **doing everything you can** to ensure that when that individual employee is facing a singular ethical challenge, he has been **informed, trained, and empowered to choose right over wrong**. Or if he makes the wrong choice, you have a **system that immediately detects, remediates, disciplines, and then adapts to make sure that others do not follow suit**."
- A well-designed/implemented compliance program provides the best chance to (i) **avoid compliance problems** in the first place, (ii) **nip potential problems in the bud** before they blossom into a full-blown crisis, and (iii) **achieve the most favorable resolution** at the close of any resulting investigation.

M&A Compliance Due Diligence and Integration

DOJ and SEC encourage risk-based due diligence to reduce risk of undisclosed misconduct, allocate costs/responsibilities, and demonstrate commitment.



M&A Compliance Due Diligence and Integration

DOJ and SEC also encourage effective compliance integration tailored to the particular transaction, such as: compliance review of acquired businesses; prompt implementation of acquirer's compliance program; and training of newly acquired personnel and agents.

INTEGRATION CHART