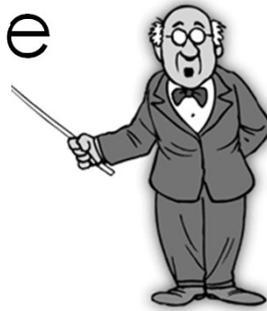


# Ethical Issues and Compliance

Ted Banks



1

## Scenario: New Employee Orientation

- Employees given copies of a very nicely designed code of conduct.
- Asked to sign a certification that they have read it, understand it, and will abide by it.
- A good thing, right?



2

2



3

What if your hotline routinely mishandled calls?

---

“Wells CEO Says the Ethics Hotline Was **Mostly** Ethical” (Nov. 11, 2016)



4

4



**Trust Me,  
I'm An Expert**

## Law Firm Website

“Our lawyers are experts in compliance and can help your company design a compliance program for [insert subject here].”

Could it be OK if it is modified by reference to a specific subject, such as the U.S. Department of Labor’s Office of Federal Contract Compliance Programs (OFCCP), the Affordable Care Act, or Medicare claims?

5

5

## Model Rule 7.4

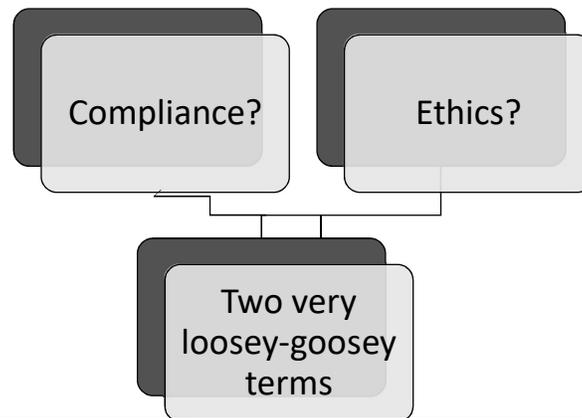


- (a) A lawyer may communicate the fact that the lawyer does or does not practice in particular fields of law . . . .
- (d) A lawyer shall not state or imply that a lawyer is certified as a specialist in a particular field of law, unless:
  - (1) the lawyer has been certified as a specialist by an organization that has been approved by an appropriate state authority or that has been accredited by the American Bar Association; and
  - (2) the name of the certifying organization is clearly identified in the communication.

6

6

What are we talking about?



7

7

## Your Ethical Obligations

- Compliance officers set the ethical example.
- Understand your definitions and your boundaries: compliance programs and ethical conduct.
- Lawyers have an ethical obligation to be ethical.
- What's happened recently?



8

## Rule 1.1 Competence

A lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation.



9

9

what are other  
words for  
legal competence?



legal capacity, active capacity,  
capacity, competence



Thesaurus.plus

Basic assumption . . .

. . . you keep up on the law.

10



## Technology and Competence – Comment 8

- ABA Model Rule: To maintain the requisite knowledge and skill, a lawyer should keep abreast of changes in the law and its practice, including the benefits and risks associated with relevant technology, engage in continuing study and education and comply with all continuing legal education requirements to which the lawyer is subject.
- Adopted in 35 states, California follows without formal adoption (8/19).

11

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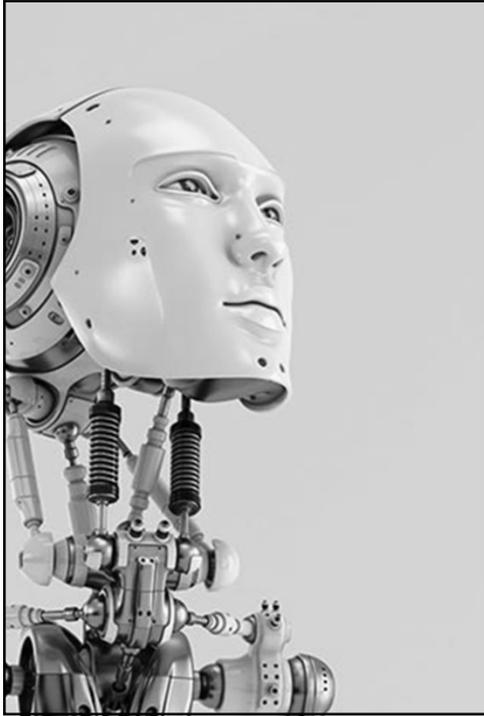


## Technology and Corporate Culture

- **Old rule: no personal computer use on the job.**
- **New: give employees social media breaks?**
  - They are going to do it anyway, so get rid of hypocrisy
  - Improves focus

12

12



## ABA Annual Meeting

August 12-13, 2019

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**Resolution 112:** RESOLVED, That the American Bar Association urges courts and lawyers to address the 1 emerging ethical and legal issues related to the usage of artificial intelligence (“AI”) in the 2 practice of law including: (1) bias, explainability, and transparency of automated decisions 3 made by AI; (2) ethical and beneficial usage of AI; and (3) controls and oversight of AI and the vendors that provide AI.

13

13

## Compliance and Ethics of AI: Good or Evil?

- Can't Use It
  - Predicting success for your firm based on track record violates Rule 7.1
  - If will produce unexplained or unexplainable results that might violate laws
  - French ban on judicial analytics
  - Risk of false positives
- Should Use It
  - SEC predicts insider trading violations
  - Antitrust Division wants screening
  - Can help detect compliance violations as it becomes more developed
  - May be required to accurately predict likelihood of success

14

14

## Rule 1.6(c) Confidentiality of Information

A lawyer shall make reasonable efforts to prevent the inadvertent or unauthorized disclosure of, or unauthorized access to, information relating to the representation of a client.

Reaffirmed in Formal Opinion  
477R (10/17): encryption  
when warranted.

No specific requirements, but a fact-based analysis with “a ‘process’ to assess risks, identify and implement appropriate security measures responsive to those risks, verify that they are effectively implemented, and ensure that they are continually updated in response to new developments.”



15

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## Comment 18: Security of Information

The unauthorized access to, or the inadvertent or unauthorized disclosure of, information relating to the representation of a client does not constitute a violation of paragraph (c) if the lawyer has made reasonable efforts to prevent the access or disclosure. Factors to be considered in determining the reasonableness of the lawyer's efforts include, but are not limited to, the sensitivity of the information, the likelihood of disclosure if additional safeguards are not employed, the cost of employing additional safeguards, the difficulty of implementing the safeguards, and the extent to which the safeguards adversely affect the lawyer's ability to represent clients (e.g., by making a device or important piece of software excessively difficult to use). A client may require the lawyer to implement special security measures not required by this Rule or may give informed consent to forgo security measures that would otherwise be required by this Rule. Whether a lawyer may be required to take additional steps to safeguard a client's information in order to comply with other law, such as state and federal laws that govern data privacy or that impose notification requirements upon the loss of, or unauthorized access to, electronic information, is beyond the scope of these Rules. For a lawyer's duties when sharing information with nonlawyers outside the lawyer's own firm, see Comments [3] and [4] to Rule 5.3.



16

16



## Technology and Compliance

- Do you have a system in place to review compliance issues each time a new type of technology is adopted? Does each system have its own ethical standards?
- To the extent you have any new technology in place, is there a way for it to communicate with people, or for people to monitor / control?

17

17

## Government Agency Ethics Rules

- FTC warning in *Competition Matters* blog (5/19): intentionally misleading the Commission could lead to “public reprimands, sanctions and even disbarment” from Commission practice.
- Most lawyers are honest, but “for a few,” there may be “perceived opportunities to seek an advantage in the debate through misrepresentation of key facts.” Some instances when “internal documents expressly contradict representations made by counsel and clients during investigations,” and “where the innocent explanation” for such inconsistencies “seemed implausible.”
- Other agencies have ethics rules, too.



18

18

## An ethical question and not much of an answer

Los Angeles Cty. Bar Ass'n Prof'l Responsibility & Ethics Comm. Op.531 (July 24, 2019)

- Can an attorney accept discovery evidence by a former employee of an opposing party that was purposely concealed?
- If documents stolen, can't accept since this is conduct that may be illegal and may require attorney to notify law enforcement.
- If not sure if stolen, check with another attorney (?) Maybe protected by privilege. Notify privilege holder.
- But sometimes evidence originating from an opposing party doesn't trigger concerns about "ethical impropriety."
  - California case: attorney may have a professional obligation to use non-privileged facts gleaned from a privileged memorandum of the opposing counsel for the benefit of the client.
  - The lawyer's duties to the client also include diligent representation, requiring the lawyer to further investigate what's in the data, the committee said.
- Lawyer facing a situation similar to this one "should conduct a thorough analysis before accepting possession of or reviewing any evidence whose provenance is uncertain."



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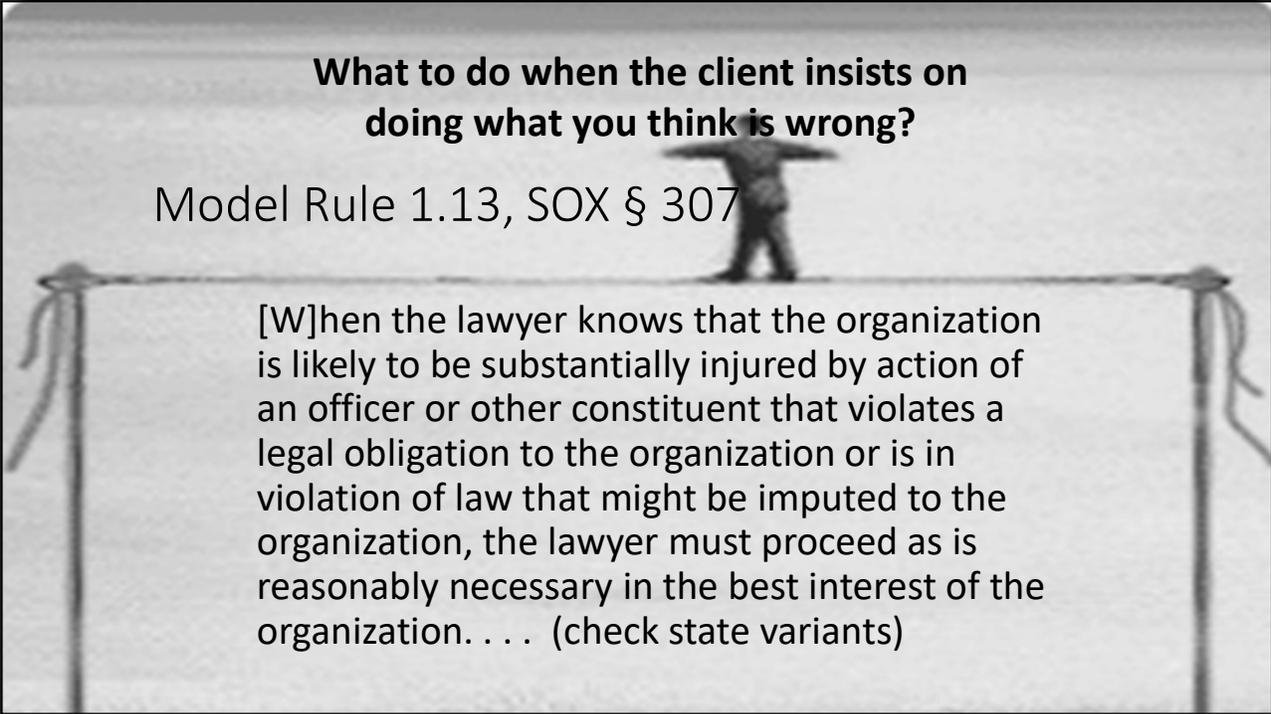
19

## Rule 1.2(d): Can't assist client in conduct known to be criminal or fraudulent

- **Gansett One, LLC v. Husch Blackwell, LLP**, N.Y. App. Div. (1/24/19) law firm to face claims it aided & abetted embezzlement scheme disguised as loans, with lawyers drafting loan documents, but not disclosed to investors.
- Comment 9: A "critical distinction between presenting an analysis of legal aspects of questionable conduct and recommending the means by which a crime or fraud might be committed with impunity."
- Marijuana illegal for all uses in only 3 states (4/19), but still illegal under Controlled Substances Act, 21 U.S.C. sec. 812(b)(1)
- ABA House of Delegates (8/19): feds should enact legislation that exempts production, distribution, possession and use of cannabis from the Act.



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## What to do when the client insists on doing what you think is wrong?

Model Rule 1.13, SOX § 307

[W]hen the lawyer knows that the organization is likely to be substantially injured by action of an officer or other constituent that violates a legal obligation to the organization or is in violation of law that might be imputed to the organization, the lawyer must proceed as is reasonably necessary in the best interest of the organization. . . . (check state variants)

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## A conflict of interest

- Rule 1.7(a)(1): The representation of one client [the entity] will be directly adverse to another client [employee]
- (a)(2): A significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer."
- Hard for in-house lawyer to tell CEO to get his own lawyer? You're fired!
- In-house lawyer assess business risk; outside counsel look at narrow legal questions.

22

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## Noisy Withdrawal?

**If, despite the lawyer's efforts in accordance with paragraph (b), the highest authority that can act on behalf of the organization insists upon action, or a refusal to act, that is clearly in violation of law and is likely to result in a substantial injury to the organization, the lawyer may reveal confidential information only if permitted by Rule 1.6, and may resign in accordance with Rule 1.16.**



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## Confidentiality

**1.6(b) A lawyer may reveal or use confidential information to the extent that the lawyer reasonably believes necessary:**

**(1) to prevent reasonably certain death or substantial bodily harm;**

**(2) to prevent the client from committing a crime;**

**(3) to withdraw a written or oral opinion or representation previously given by the lawyer and reasonably believed by the lawyer still to be relied upon by a third person, where the lawyer has discovered that the opinion or representation was based on materially inaccurate information or is being used to further a crime or fraud; . . .**

**(5)(ii) to establish or collect a fee . . .**

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## Can GC be Whistleblower? *Wadler v. Bio-Rad Laboratories*



- Alleged termination for submitting memo to audit committee regarding FCPA violations was illegal retaliation for whistleblowing under SOX, Dodd-Frank and California common law
- Amicus brief #1 from SEC: Dodd-Frank prohibits retaliation based on internal complaints. Motion to dismiss denied.
- Motion to exclude privileged evidence generates amicus brief #2 from SEC:
  - purpose of federal laws to protect all employees of public companies from retaliation
  - SOX preempts Calif. ethical rules regarding disclosure of privileged info
- Motion denied; trial Jan. – Feb. 2017
- Jury (Feb. 2017): \$11 million awarded for whistleblower retaliation
- Judgment confirmed (May 2017)
- Appealed . . .

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## Wadler v. Bio-Rad

No. 17-cv-16193 (9<sup>th</sup> Cir. Feb. 26, 2019)

- Upheld award of damages under Calif. law, but:
- Can't recover double backpay under Dodd-Frank, since it doesn't cover purely internal complaints. *Digital Realty Trust, Inc. v. Somers, No. 10-1276 (U.S. 2018)*
- Vacated SOX claim, since FCPA not considered "rules or regulations" of SEC under SOX §806 (differentiating between laws and regulations based on statutory language).
- Remanded to consider if new trial needed based on erroneous ITJ.
- **No ruling on the use of privileged information at trial**



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## Erhart v. Bofi Holding, Inc.,

269 F. Supp. 3<sup>rd</sup> 1059 (S.D. Cal. Sept. 11, 2017)



- Internal auditor filed whistleblower retaliation claim under SOX & Dodd-Frank.
  - Counterclaim of violation of Calif. Law by sharing confidential information with N.Y. Times and deleting emails from laptop
  - Stock price plummets
- Erhart notified SEC that Bank had falsely answered SEC subpoena, and other matters reported to SEC and OCC
- Employee covered by SOX if
  - “Reasonably believes” conduct was a violation
  - Employer knew or suspected protected activity
  - Employee suffers adverse action
  - Protected activity contributed to adverse action (inference based on temporal proximity)

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## Erhart v. Bofi (cont'd)

- Allegations already reported in N.Y. Times, so court would not review whether Erhart violated “some privilege or right of privacy.”
- Erhart permitted to disclose information if “reasonably necessary” to pursue retaliation claim.
  - Strong public policy in favor of protecting whistleblower who report fraud against the government.
  - **Citing Wadler** and *Ruhe v. Masimo Corp.*, 929 F. Supp. 2d 1033, 1039 (C.D. Cal. 2012).
- No. 15-cv-02287 (S.D. Cal. Apr. 30, 2019):
  - No ruling on the pleadings with regard to whether Erhart exhausted SOX administrative remedies
  - Erhart plausibly alleged SOX whistleblower retaliation claim
  - Case continues

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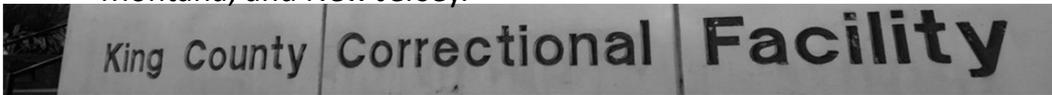
28

## In-House Counsel Can Sue Employer For Firing

### *Karstetter v. King Cty. Corr. Guild*

No. 95531-0 (Wash. July 18, 2019)

- Case alleged violation of contract requiring just cause for termination.
- Wash. Sup. Ct. concluded that in-house attorneys may pursue wrongful discharge and breach of contract claims against their client-employers. Plaintiff's claims should not have been dismissed. Sufficient facts pleaded to bring the claims.
- Court notes evolving nature of attorney jobs and rejects "rigid interpretation" of legal ethics rule that allows client to fire lawyer for any reason at any time. In-house counsel have legal & nonlegal duties.
- "Solely in the narrow context of in-house employee attorneys, contract and wrongful discharge suits are available, provided these suits can be brought without violence to the integrity of the attorney-client relationship."
- Similar action can be brought in California, Massachusetts, Minnesota, Montana, and New Jersey.



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## The New York Times

### *Ex-Department of Justice Lawyer Faces Penalties in Leak of N.S.A. Program*

WASHINGTON — <sup>Jan. 17, 2016</sup> The District of Columbia bar is pursuing ethics charges against a former Department of Justice lawyer who has said he was one of the sources for a 2005 article in The New York Times about the National Security Agency's program of wiretapping without warrants.

- Lawyer concerned that certain warrants received "special Treatment" at FISA Court that violated the law
- Admitted violation of Rule 1.6, accepted public censure. In re Tamm, No. 16-BG-690 (D.C. Aug. 25, 2016)
- Mitigating circumstances:
  - Cooperation with disciplinary counsel
  - Intent to further compliance with law
  - Disclosure was limited
  - No financial compensation for disclosure
  - Investigation was stressful and expensive

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## You cannot ignore the obvious



Rule 1.0(k)[or 1.0(f)]:  
knowledge can be  
inferred from  
circumstances

31

## Federal Sentencing Guidelines: “Willfully Ignorant”

“An individual was ‘willfully ignorant of the offense’ if the individual did not investigate the possible occurrence of unlawful conduct despite knowledge of circumstances that would lead a reasonable person to investigate whether unlawful conduct had occurred”.



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## Federal Sentencing Guidelines: Promptly Report

. . . the organization will be allowed a reasonable period of time to conduct an internal investigation. In addition, no reporting is required . . . if the organization reasonably concluded, based on the information then available, that no offense had been committed.



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## Advocate or Conscience?

- Model Rule 2.1
  - Exercise your independent professional judgment.
  - In addition to law, consider moral, economic, social, psychological, and political factors
- NY Rule 2.1 Comment [2]
  - It is proper for a lawyer to refer to relevant moral and ethical considerations in giving advice. Although a lawyer is not a moral advisor as such, moral and ethical considerations impinge upon most legal questions and may decisively influence how the law will be applied.
- Model Rule 3.1
  - No frivolous actions, but
  - Can defend vigorously



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## What kind of advice did this lawyer provide?

- Turing Pharmaceuticals outside counsel and corporate secretary, Evan Greebel, convicted of wire fraud and securities fraud.
  - 18 months in prison + \$10.5 million restitution.
  - Judge: he was “personally generous and kind” but he “abused his position of trust”
  - Too broad definition of “duty” argued on appeal, only had to talk to CEO (Shkreli)
- Turing Pharmaceuticals and its CEO, Martin Shkreli, attracts attention by increasing price of drug by more than 5000% and general arrogance
  - Shkreli convicted of defrauding investors in hedge funds (7 years in prison)
  - July 18, 2019: 2d Cir. affirms conviction. Can commit fraud even if investors didn’t lose money.
- Gatekeeper concept: those with a direct, formal governance authority
  - In-house lawyer should serve as “gatekeeper” to protect company
  - Also includes directors, public accounting firms, outside counsel
- Spring Pharm. LLC v. Retrophin, Inc. (E.D. Pa. Apr. 10, 2019)
  - Refusal to dismiss antitrust case
  - Shkreli placed in solitary confinement for using unauthorized cellphone
- Shkreli v. Yaffe , No. 19-cv-5084 (E.D.N.Y. filed Sept. 6, 2019)
  - Shkreli Files suit from prison against former business associate and prosecution witness.
  - Claimed that \$250,000 promissory note is now unenforceable



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## Rule 8.4: Misconduct

### **Maintaining The Integrity Of The Profession** **Rule 8.4 Misconduct**

It is professional misconduct for a lawyer to:

- . . . (g) engage in conduct that the lawyer knows or reasonably should know is harassment or discrimination on the basis of race, sex, religion, national origin, ethnicity, disability, age, sexual orientation, gender identity, marital status or socioeconomic status in conduct related to the practice of law. This paragraph does not limit the ability of a lawyer to accept, decline or withdraw from a representation in accordance with Rule 1.16. This paragraph does not preclude legitimate advice or advocacy consistent with these Rules.

Adopted 8/16 by ABA house of Delegates by overwhelming majority. But opposed in many states.

Opposition by Christian Legal Society and Federalist Society. Argument: NIFLA v. Becerra (6/18) ruled that there were no rules for “professional speech.” All regulations based on the content of speech subject to strict scrutiny. More leeway to regulate conduct that incidentally involves speech.



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## Is it legal advice or legal evasion?

N.Y.S. Bar Ass'n Comm. on Prof'l Ethics,  
Op.1171 (Aug. 26, 2019).



- Rule 8.4(c) of the New York Rules of Professional Conduct prohibits lawyers from engaging in conduct involving dishonesty, fraud, deceit, or misrepresentation.
- Question: Can a client use attorney' escrow account to avoid direct payment from a Chinese client to a U.S. company in violation of Chinese currency controls?
- Answer: No. Goal of the proposed transaction "would be to disguise the true nature of the money transfers and deceive government authorities and counter-parties", in violation of the ethics rule.
- Not sure if the act would violate Rule 1.2(b), which deals with helping clients engage in fraudulent conduct, or Rule 8.4(b), which deals with acts reflecting adversely on a lawyer's fitness, since not clear whether these rules extend to conduct illegal in another country.

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## Unethical Investigations?

Colorado Opinion 137 (May 2019)

- Rule 8.4(c) provides it is professional misconduct for a lawyer to "engage in conduct involving dishonesty, fraud, deceit or misrepresentation, except that a lawyer may advise, direct, or supervise others, including clients, law enforcement officers, or investigators, who participate in lawful investigative activities."
- Criminal investigation: can use fraud, deceit, and misrep. as long as no misleading of courts
- Civil invest: can use deceit, like posing as members of public, as long as no attempt to induce subject to do something otherwise would not
- Lawyers cannot themselves engage in deceit

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## Code of Ethics for Compliance & Ethics Professionals

- Obey spirit and letter of the law (prevent misconduct, cooperation, take action if aware of misconduct)
- Serve employing organizations with highest sense of integrity (assist in complying with law, investigate allegations, advise senior management, no retaliation, confidentiality, no conflicts of interest)
- Strive to uphold integrity and dignity of the profession (act with honesty, protect confidentiality, no false statements, maintain education)
- [Full text at end]

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- Legal advice
  - Communication within scope of duties
  - For purpose of obtaining legal (not business) advice
- Work product: Is litigation anticipated?
- Self-Evaluative Privilege: Nope

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## Privilege and M&A

*Shareholder Representative Services LLC v. RSI Holdco, LLC, C.A. No. 2018-0517-KSJM (Del. Ch. May 29, 2019).*

- Merger agreement provided that seller's privilege "shall remain in effect," that it "shall be assigned" to the selling stockholders' representative, and that neither party could "use or rely on any of the Privileged Communications in any action or claim against or involving any of the parties" to the agreement.
  - Buyer took possession of all files including privileged communications.
  - Buyer asserted right to use privileged communications against seller.
- Ct: Privileges are usually transferred in mergers
  - However, contractually you can prevent that from happening
  - Failure to segregate and remove privileged information does not waive privilege

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## Barko v. Halliburton (D.D.C. 2014), *rev'd*, *In re Kellogg Brown & Root* (D.C. Cir. 2015)



- No attorney-client privilege or work product protection for investigation conducted by Office of Business Conduct
  - Investigation required by law and corporate policy, not for purpose of obtaining legal advice
  - Investigation conducted by non-lawyers
- Reversed: investigation to obtain facts and ensure compliance with law
  - Conducted under auspices of legal department acting in legal capacity
- Involve lawyers in investigations at early stage
  - Investigators should report to lawyers
  - Can disclose nonprivileged facts without waiving privilege

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## Must employees cooperate with investigations?

*United States v. Connelly*  
16 Cr. 370 (S.D.N.Y. 5/2/19)

- Defendant convicted of LIBOR-rigging argued for acquittal as a violation of his 5th Amend. rights since his cooperation in an internal investigation was coerced by the threat of termination and the firm was actually acting for the government.
- CT: DOJ had improperly outsourced its investigation to the bank and its outside law firm.
- Level of government involvement in the “internal” investigation, combined with little independent investigation by DOJ resulted in finding that the bank and its counsel “were de facto the Government.”
- *Garrity v. N.J.* (U.S. 1967): statements from employee threatened with firing were infected by coercion and inadmissible against them.
- *U.S. v. Stein* (2d Cir. 2008): apply Garrity rule if conduct of private actor is “fairly attributable to the government.”
- Company counsel have basis to resist government management of investigations; don’t need to let government get involved at all; carefully document all internal decisions about investigation; perhaps counsel for employee

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## Does a malpractice claim defeat privilege?

*Murray Energy Corp. v. Cassidy, Cogan, Chappell & Voegelin, L.C.*, No. 2:18- cv-440  
(S.D. Ohio, July 29, 2019)

- Law firm confidentially settles two cases of women alleging sexual harassment by CEO.
- Same firm represents another woman, mentions claims of first 2 women in demand letter.
- Suit against law firm alleges breach of confidential settlement agreement and legal malpractice. Sought production of case files and notes of discussions with three clients.
- Discovery request denied. Violation of ethical obligation to maintain confidentiality would not require production of information. Not a violation of ethical rules, and no privilege waiver.

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## Are compliance programs privileged?

- Should they be?



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## Domestic Drywall-Antitrust Litigation

— MDL No. 2437 (E.D. Pa. Oct. 9, 2014)

- **Defendant seeks to prevent discovery of compliance program, arguing that it met the technical requirements for privilege (a communication maintained in confidence for the purpose of providing legal advice between privileged persons).**
- **The court disagreed**
  - privilege limited to legal advice leading to a decision by the client.
  - antitrust program was general, did not contain any specific advice, was more akin to a reference or instructional guide, and was primarily a business policy.
  - policy not maintained in confidence
    - distributed to more than 120 employees
    - posted on an intranet site
    - not labeled as confidential or privileged.

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## In re Sulfuric Acid Antitrust Litigation

235 F.R.D. 407 (N.D. Ill. 2006) and 432 F. Supp. 2d 794 (N.D. Ill. 2006)

- Antitrust compliance manuals contained a series of hypothetical questions posed that were distributed to marketing, sales, and production management employees
- Certain portions of compliance manuals not privileged, since they did not reveal client confidences and were nothing more than an articulation of company policies
- (These) hypotheticals not privileged
  - influenced by historic cases or were entirely the product of counsel's imagination.
  - Ct: like giving a talk on experiences or writing an article on antitrust concerns to the sulfuric acid industry.
  - Did not contain any client confidences



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## In re Loestrin 24 Fe Antitrust Lit.

MDL No. 2472 (D.R.I. Nov. 29, 2017)

- Request to produce all policies, all versions, whenever created, related to antitrust compliance and business conduct or ethics standards.
- Court limits production based on time period surrounding formation of agreements at issue, instead of back to the beginning of time.



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## Miller v. Smith Barney

No. 84 Civ. 4307, 1986 U.S. Dist. LEXIS 28787, Fed. Sec. L. Rep. ¶ 92,498 (S.D.N.Y. Feb. 27, 1986).



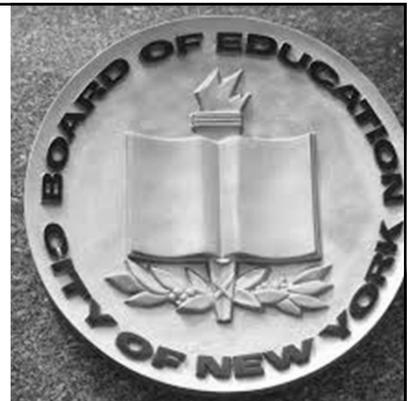
- Internal compliance manuals were not privileged
  - Disclosed in prior litigation
  - Required to be maintained by the NYSE and NASD (and thus could not be deemed confidential)
  - As a compendium of operating procedures and rules, not considered to be legal opinions.
- The fact that they were authored by an attorney was not the test of the privilege's applicability.

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## O'Brien v. Board of Ed. of New York

86 F.R.D. 548 (S.D.N.Y. 1980)



- Hypothetical questions were put to counsel
- The answers revealed the mental processes of the clients and various alternative strategies, all of which was entitled to protection

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ABA: Can't avoid confidentiality rule by claiming scenarios are theoretical if they aren't <sup>(3/18)</sup>

- Rule 1.6 might provide an exception for information that is publicly and generally known
- “A violation of Rule 1.6(a) is not avoided by describing public commentary as a ‘hypothetical’ if there is a reasonable likelihood that a third party may ascertain the identity or situation of the client from the facts set forth in the hypothetical.”
- “Hence, if a lawyer uses a hypothetical when offering public commentary, the hypothetical should be constructed so that there is no such likelihood.”



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Is a compliance program evidence of anything?

- Not the law: The judge instructed the jury.
- Can't admit the compliance program since might mislead jury
- *MM Steel LP v. Reliance Steel & Aluminum Co.*, No. 4:12-cv-1227 (S.D. Tex. Dec. 16, 2013), *citing* *United States v. North*, 2007 WL 1630366 (D. Conn. June 5, 2007).



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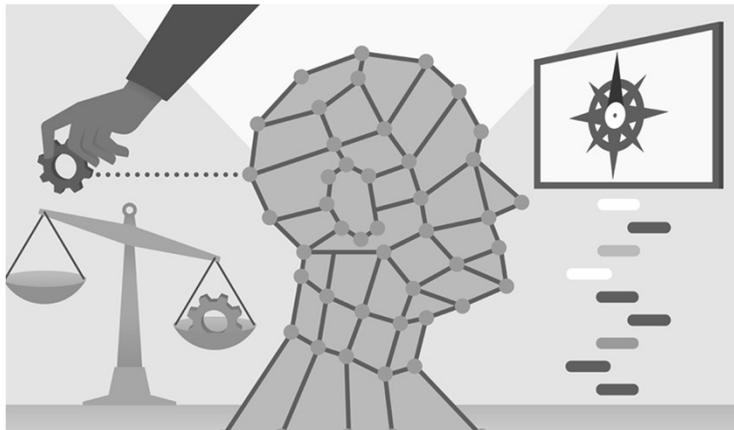
## “Attorney” Communications not Legal Advice

SEC v. Alderson, No. 18-cv-04930 (S.D.N.Y. June 10, 2019).

- Investment advisers accused of misleading clients claimed they relied in good faith on advice of counsel, and refused to turn over docs
- Compliance questions handled by consulting firm staffed by attorneys, expressly disclaiming atty/client rel.
- Same attorneys also worked for law firm (more expensive), but clients told that documents created at consulting firm were not legal advice.
- Company ordered to turn over compliance communications.

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**Privilege and Public Relations**  
In re Signet Jewelers Ltd. Sec. Litig., No. 16-cv-6728 (S.D.N.Y. Sept. 5, 2019).

- Must disclose some attorneys' communications with outside public relations firms in a shareholders' suit alleging concealment of a culture of sexual harassment.
  - PR firm hired to “discuss a communications strategy.” Was it for legal advice?
  - Some documents might be protected as work product.
- Think: What about using a PR firm to advise how to improve corporate culture?

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## Previously: Antitrust Division Didn't Like to Give Credit for Compliance Programs



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Hints that things might be changing . . .

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## Roundtable on Criminal Antitrust Compliance

April 9, 2018

- “Corporate compliance is key to the Antitrust Division's ultimate goals of preventing and uncovering criminal antitrust violations and protecting consumers and small businesses,” said Assistant Attorney General Makan Delrahim.
- Buenos Aires (April 10, 2019): still considering how to credit compliance



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## Evaluation of Corporate Compliance Programs in Criminal Antitrust Investigations

July 11, 2019

- Follow the Sentencing Guidelines
- Three fundamental questions:
  - Is the corporation's compliance program well designed?
  - Is the program being applied earnestly and in good faith?
  - Does the corporation's compliance program work?
- Efficacy of the compliance program:
  - Does the company's compliance program address and prohibit criminal antitrust violations?
  - Did the antitrust compliance program detect and facilitate prompt reporting of the violation?
  - To what extent was a company's senior management involved in the violation?

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## Evaluation of Corporate Compliance Programs in Criminal Antitrust Investigations (cont'd)

- Essential analysis factors (with subparts)
  - the design and comprehensiveness of the program;
  - the culture of compliance within the company;
  - responsibility for, and resources dedicated to, antitrust compliance;
  - antitrust risk assessment techniques;
  - compliance training and communication to employees;
  - monitoring and auditing techniques, including continued review, evaluation, and revision of the antitrust compliance program;
    - Does the company use any type of screen, communications monitoring tool, or statistical testing designed to identify potential antitrust violations? [AI?]
  - reporting mechanisms;
  - compliance incentives and discipline; and
  - remediation methods
- **Follow the Sentencing Guidelines**

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## Compliance Officer Can be Part of the Violation

- Robert Riley, VP Regulatory Affairs & Chief Compliance Officer of AbTox, Inc.
- Submitted false or misleading data regarding safety of sterilizer units.
- Judge Castillo in *United States v. Caputo*, 456 F. Supp. 2d 970, 984-85 (N.D. Ill. 2006):



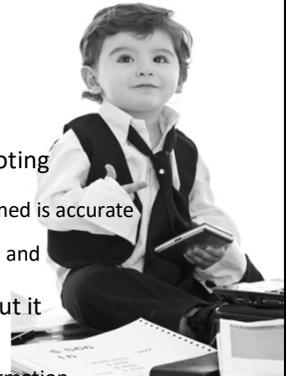
“Caputo selected Riley to serve as AbTox's Chief Compliance Officer for all the wrong reasons. Caputo knew that he could manipulate and dominate Riley based on his prior personal and business experiences with him. Riley did not have any real training as a compliance officer. . . . Riley aided and abetted Caputo's illegal marketing plans. Riley chose to use whatever regulatory expertise he had to further, shield, and cover up the offenses proven at trial.”

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## Inexperienced Compliance Officer?

- Broker-dealers must review and maintain information about an issuer before quoting for an OTC and non-exchange listed security. (Rule 15c2-11 of the Exchange Act)
  - Broker-dealer must have a reasonable basis for believing that the information it has obtained is accurate and reliable.
  - Broker-dealer to demonstrate compliance with the Rule by filing the Form 211, reviewed and signed by a principal of the firm. (FINRA Rule 6432)
- Canaccord Genuity LLC had written policies and procedures covering the rules, but it failed to follow its written policies and procedures and violated the rules, according to an SEC order.
  - Assigned a compliance associate the responsibility to obtain and review the required information.
  - The associate filled out the Form 211s and placed the electronic signature of the designated principal on the filings.
  - The files were in a compliance filing cabinet that could not be independently accessed by the traders or the firm's designated principal without requesting them from the compliance department.
- Per the SEC in imposing a penalty on the firm: "The compliance associate had no trading experience and no formal training to conduct the review required by the rule, such as training related to the analysis of financial statements and other information."
- Was the compliance associate aware of the law, the company policy and the violation? (Thanks to Doug Cornelius)



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## Corporate Manager Can be Liable: *Texas v. Morello*

547 S.W. 3d 881 (Tex. Feb. 23, 2018)

- State sued member/manager of LLC for violations of Texas Water Code (groundwater contamination) based on LLC's failure to satisfy compliance plan accompanying its hazardous waste permit.
- Tex. Ct. App.: Liability protection under Tex. Bus. Org. Code. State failed to show that failures to satisfy compliance plan were the type of "tortious or fraudulent" acts for which corp. officers can be held personally liable
- Tex. S. Ct.: Rev'd. Notwithstanding statutory language, this individual liable based on both the Water Code and the individual's own actions, which subject him to liability regardless of whether he was acting as an agent of the LLC.



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## Auditor Liability: Regulatory Fraud

U.S. v. Middendorf, No. 1:18-cr-00036 (S.D.N.Y. Sept. 11, 2019).

- David Mittendorf (KPMG) convicted of wire fraud and conspiracy for getting “inside” information from current and former PCAOB staffers on what companies’ audits would be inspected. Audit work altered
  - PCAOB inspection lists were “property” under the wire fraud statute.
  - Defense: I made mistakes, not crimes
- Not a typical fraud where a defendant personally benefitted, but corruption of the regulatory process justified year-and-a-day sentence. \$50 million SEC fine
- AUSA wanted tougher sentence: give him 3 years since position as national managing partner for audit quality and professional practice meant that conduct “threatened to infect the entire firm.”
  - August 2019: Another KPMG partner sentenced to 8 months for same conduct.
  - Another KPMG partner going to trial Oct. 21. Others also accused.
- But don’t worry, as a Tweet noted, “we’re sure the rest of those audits are all just fine.”



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## Attorney Personal Liability for Fraud

Fifth Third Mort. Co. v. Kaufman, No. 18-03295 (Aug. 9, 2019)

- Numerous fraudulent mortgage applications by seller’s attorney and owner of the title company used in the closings.
- Argued: Illinois law shields individuals for wrongs committed in their capacity as LLC members
- 7<sup>th</sup> Cir: Found liable for individual acts:
  - Directed title co. employees to conceal fraud from bank
  - Appeared at closings as counsel for seller



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## Is GC of Hertz Liabile for Accounting Problems?

*The Hertz Corp. v. Frissora*, No. 2:19-cv-08927 (D.N.J.)



Mark Frissora

- Complaint (March 25, 2019) alleges failure by ex-GC John Zimmerman to ensure compliance with reporting obligations. CEO & CFO also sued. \$200 million + \$70 million clawback. Misstatements on separation agreement?
- Accounting errors resulted in \$16 million settlement with SEC.
- Tone at the top matters: CEO pressured subordinates to use “paradigm-busting” accounting strategies that resulted in inappropriate accounting decisions.
- Mot. to Dismiss (June 2019): complaint did not provide specific examples of Zimmerman’s failures, just a general failure to counter-balance tone at the top.

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## Lawyer as Compliance Officer?

- How do things get done?
- Lawyer can make noisy withdrawal. Can others?
- HHS: GC can’t be compliance officer



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Lawyer as your gladiator?



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## Poster Children: Violation Based on the “Compliance Officer” Title and Careless Attestations

- Mark Kipnis – Hollinger
  - 2007 – Conrad Black and others convicted
  - Kipnis did not get any money from the fraud
  - Judge Amy St. Eve: Kipnis was “clearly the least culpable person in his scheme”
  - No jail, but 5 years probation, loss of law license.
  - 2010: S. Ct. overturns convictions based on “honest services fraud”
- Christi Sulzbach – Tenet
  - Resigned 2003
  - Litigation continued until 2010
  - But took home huge compensation



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## Theranos and Its Counsel

- Blood testing device never worked
- Board members never inquired
- David Boies (attorney & board member) used intimidation to stop Theranos whistleblowers
- Previously worked to suppress stories about Harvey Weinstein including hiring undercover investigators to investigate reporters

“You don’t know all the facts when you take on a client . . . but once you do, you have a duty of loyalty. You can’t represent them halfway. If, as a lawyer you start to value how you are going to look to the media, as opposed to how your client will look, then you should find a new profession.”

J. Stewart, “David Boies Pleads His Own Case,” N.Y. Times (Sept. 23, 2018)

- “They lied to us.” Former Walgreen’s General Counsel at SCCE Regional Conference (May 3, 2019)



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## Lawyers, CCOs and Compliance

- Competence in compliance essential
- Need not be subject matter expert in everything, but never pretend to understand something you don’t
- Compliance officer, lawyer or not, should be an ethical gatekeeper
- This is key to a CCO’s strength
  - Be politically savvy, but don’t let concern about image be more important than ethics
  - An ethical “stand your ground” law needed?

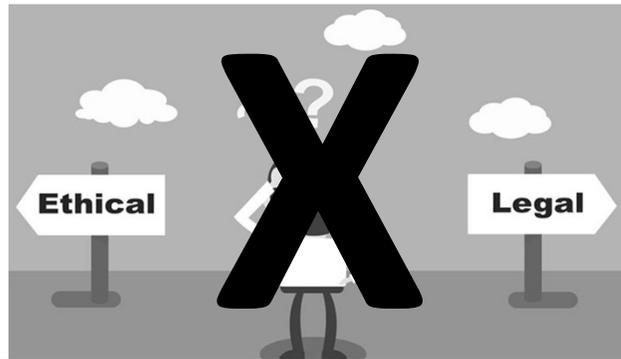


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## Make sure you ask the right questions

- It is not “ethical vs. legal”
- It is right vs. wrong, or smart vs. stupid
- Make sure you know how to be smart.



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*Thank you!*

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# Code of Professional Ethics for Compliance and Ethics Professionals

## Society of Corporate Compliance & Ethics

### **Principle 1: Obligations to the Public**

Compliance and ethics professionals (CEPs) should abide by and promote compliance with the spirit and the letter of the law governing their employing organization's conduct and exemplify the highest ethical standards in their professional conduct in order to contribute to the public good.

**R1.1** CEPs shall not aid, abet or participate in misconduct.

**R1.2** CEPs shall take such steps as are necessary to prevent misconduct by their employing organizations.

**Commentary:** *The CEP's actions to prevent misconduct must, of course, be legal and ethical. Where a CEP has done what he or she can to prevent misconduct within the bounds of the law and business ethics, but is nonetheless unsuccessful in preventing misconduct, he or she should refer to Rule 1.4.*

**R1.3** CEPs shall exercise sound judgment in responding to or cooperating with all official and legitimate government investigations of or inquiries concerning their employing organization.

**Commentary:** *While the role of the CEP in a government investigation may vary, the CEP shall never obstruct or lie in an investigation.*

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## SCCE Ethics Code (cont'd.)

**R1.4** If, in the course of their work, CEPs become aware of any decision by their employing organization which, if implemented, would constitute misconduct, the professional shall: (a) refuse to consent to the decision; (b) escalate the matter, including to the highest governing body, as appropriate; (c) if serious issues remain unresolved after exercising "a" and "b", consider resignation; and (d) report the decision to public officials when required by law.

**Commentary:** *The duty of a compliance and ethics professional goes beyond a duty to the employing organization, inasmuch as his/her duty to the public and to the profession includes prevention of organizational misconduct. The CEP should exhaust all internal means available to deter his/her employing organization, its employees and agents from engaging in misconduct. The CEP should escalate matters to the highest governing body as appropriate, including whenever: a) directed to do so by that body, e.g., by a board resolution; b) escalation to management has proved ineffective; or c) the CEP believes escalation to management would be futile. CEPs should consider resignation only as a last resort, since CEPs may be the only remaining barrier to misconduct. A letter of resignation should set forth to senior management and the highest governing body of the employing organization in full detail and with complete candor all of the conditions that necessitate his/her action. In complex organizations, the highest governing body may be the highest governing body of a parent corporation.*

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## SCCE Ethics Code (cont'd.)

### Principle II: Obligations to the Employing Organization

Compliance and ethics professionals (CEPs) should serve their employing organizations with the highest sense of integrity, exercise unprejudiced and unbiased judgment on their behalf, and promote effective compliance and ethics programs.

**R2.1** CEPs shall serve their employing organizations in a timely, competent and professional manner.

**Commentary:** *CEPs are not expected to be experts in every field of knowledge that may contribute to an effective compliance and ethics program. CEPs venturing into areas that require additional expertise shall obtain that expertise by additional education, training or through working with others with such expertise. CEPs shall have current and general knowledge of all relevant fields of knowledge that reasonably might be expected of a compliance and ethics professional, and shall take steps to ensure that they remain current by pursuing opportunities for continuing education and professional development.*

**R2.2** CEPs shall ensure to the best of their abilities that employing organizations comply with all relevant laws.

**Commentary:** *While CEPs should exercise a leadership role in compliance assurance, all employees have the responsibility to ensure compliance.*

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## SCCE Ethics Code (cont'd.)

**R2.3** CEPs shall investigate with appropriate due diligence all issues, information, reports and/or conduct that relates to actual or suspected misconduct, whether past, current or prospective.

**Commentary:** *In organizations where other professionals (such as the Legal Department) are responsible for investigation of suspected misconduct, CEPs satisfy this Rule by reporting suspected misconduct to such professionals in accordance with established reporting procedures.*

**R2.4** CEPs shall keep senior management and the highest governing body informed of the status of the compliance and ethics program, both as to the implementation of the program and about areas of compliance risk.

**Commentary:** *The CEP's ethical duty under this rule complements the duty of senior management and the highest governing body to assure themselves "that information and reporting systems exist in the organization that are reasonably designed to provide to senior management and to the board itself timely, accurate information sufficient to allow management and the board, each within its scope, to reach informed judgments concerning both the corporation's compliance with law and its business performance." In re Caremark International Inc., Derivative Litigation, 1996 WL 549894, at 8 (Del. Ch. Sept. 25, 1996)*

**R2.5** CEPs shall not aid or abet retaliation against any employee who reports actual, potential or suspected misconduct, and shall strive to implement procedures that ensure the protection from retaliation of any employee who reports actual, potential or suspected misconduct.

**Commentary:** *CEPs should preserve to the best of their ability, consistent with other duties imposed on them by this Code of Ethics, the anonymity of reporting employees, if such employees request anonymity. Further, they shall conduct the investigation of any actual, potential or suspected misconduct with utmost discretion, being careful to protect the reputations and identities of those being investigated.*

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## SCCE Ethics Code (cont'd.)

**R2.6** CEPs shall carefully guard against disclosure of confidential information obtained in the course of their professional activities, recognizing that under certain circumstances confidentiality must yield to other values or concerns, e.g., to stop an act which creates appreciable risk to health and safety, or to reveal a confidence when necessary to comply with a subpoena or other legal process.

**Commentary:** *It is not necessary to reveal confidential information to comply with a subpoena or legal process if the communications are protected by a legally recognized privilege (e.g., attorney client privilege).*

**R2.7** CEPs shall take care to avoid any actual, potential or perceived conflicts between the interests of the employing organization and either the CEP's own interests or the interests of individuals or organizations outside the employing organization with whom the CEP has a relationship. CEPs must disclose and ethically handle conflicts of interest and must remove significant conflicts whenever possible. Conflicts of interest may create divided loyalties. CEPs shall not permit loyalty to individuals in the employing organization with whom they have developed a professional or a personal relationship to interfere with or supersede the duty of loyalty to the employing organization and/or the superior responsibility of upholding the law, ethical business conduct and this Code of Ethics.

**Commentary:** *If CEPs have any business association, direct or indirect financial interest, or other interest that could influence their judgment in connection with their performance as a professional, the CEPs shall fully disclose to their employing organizations the nature of the business association, financial interest, or other interest. If a report, investigation or inquiry into misconduct relates directly or indirectly to activity in which the CEP was involved in any manner, the CEP must disclose in writing the precise nature of that involvement to the senior management of the employing organization before responding to a report or beginning an investigation or inquiry into such matter, and must recuse him or herself from such investigation or inquiry, if appropriate. Despite this requirement, such involvement in a matter subject to a report, investigation or inquiry will not necessarily prejudice the CEP's ability to fulfill his/her responsibilities in that regard.*

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## SCCE Ethics Code (cont'd.)

**R2.8** CEPs shall not mislead employing organizations about the results that can be achieved through the use of their services.

**Commentary:** *CEPs should not create unreasonable expectations with respect to the impact or results of their services.*

### **Principle III: Obligations to the Profession**

Compliance and ethics professionals (CEPs) should strive, through their actions, to uphold the integrity and dignity of the profession, to advance the effectiveness of compliance and ethics programs and to promote professionalism in compliance and ethics.

**R3.1** CEPs shall pursue their professional activities, including investigations of misconduct, with honesty, fairness and diligence.

**Commentary:** *CEPs shall not agree to unreasonable limits that would interfere with their professional ethical and legal responsibilities. Reasonable limits include those that are imposed by the employing organization's resources. If management of the employing organization requests an investigation but limits access to relevant information, CEPs shall decline the assignment and provide an explanation to the highest governing authority of the employing organization. CEPs should diligently strive to promote the most effective means to achieve compliance.*

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## SCCE Ethics Code (cont'd.)

**R3.2** Consistent with Rule 2.6, CEPs shall not disclose without consent or compulsory legal process confidential information about the business affairs or technical processes of any present or former employing organization. Such disclosure could erode trust in the profession or impair the ability of compliance and ethics professionals to obtain such information from others in the future.

**Commentary:** CEPs need free access to information to function effectively and need the ability to communicate openly with any employee or agent of an employing organization. Open communication depends upon trust. Misuse and abuse of the work product of compliance and ethics professionals poses a serious threat to compliance and ethics programs. CEPs shall not use confidential information in any way that violates the law or their legal duties, including duties to their employing organizations. When adversaries in litigation use an organization's own self-policing work against it, the credibility of CEPs may be undermined. CEPs are encouraged to work with legal counsel to protect confidentiality and to minimize litigation risks. It is not necessary to reveal confidential information to comply with compulsory legal process if the confidential information is protected by a legally recognized privilege (e.g., attorney client privilege).

**R3.3** CEPs shall not make misleading, deceptive or false statements or claims about their professional qualifications, experience or performance.

**R3.4** CEPs shall not attempt to falsely damage the professional reputation of other compliance and ethics professionals.

**Commentary:** In order to promote collegiality and civility in the profession, CEPs shall not make any statements concerning other CEPs that are defamatory in nature.

**R3.5** CEPs shall maintain their competence with respect to developments within the profession, including knowledge of and familiarity with current theories, industry practices, and laws.

**Commentary:** CEPs shall pursue a reasonable and appropriate course of continuing education, including but not limited to review of relevant professional and industry journals and publications, communication with professional colleagues and participation in open professional dialogues and exchanges through attendance at conferences and membership in professional associations