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IN-HOUSE **FOCUS**

MITIGATING FRAUD & CORRUPTION

The Main Chorus: Accountability

Avoiding Responsibility for Fraud Is Becoming a Thing of the Past

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THINKSTOCK

THE DAYS OF INDIVIDUAL EXECUTIVES avoiding responsibility for corporate fraud through the payment of massive corporate penalties (paid with shareholder dollars) are ending. From Congress to Main Street, the chorus of calls for individual prosecutions related to corporate fraud—particularly on "Wall Street"—is only getting louder.

Their consternation is not unfounded.

Incredibly, in the wake of the 2008 financial crisis, only one Wall Street executive was sent to jail. Kareem Serageldin, a senior trader at Credit Suisse, was sentenced to a 30-month prison sentence for falsely inflating the value of the mortgage bonds in his trading portfolio. Meanwhile, 49 financial institutions have paid the government and private plaintiffs nearly $140 billion in fines and settlements. In contrast, in the aftermath of the savings-and-loan crisis of the 1980s, more than 1,000 bankers were prosecuted, convicted and incarcerated for their role in the crisis.

The Department of Justice has answered the call for individual accountability by fundamentally shifting its approach to corporate misconduct. The DOJ has announced it will increasingly focus on individuals involved in corporate misconduct and offer leniency in exchange for assistance ferreting out the misconduct

to the highest levels within a target corporation.

Last fall, in fact, Deputy Attorney General Sally Quinlan Yates issued a memorandum to all federal prosecutors mandating that corporate cooperation credit now requires a corporation to provide full and complete information about all individuals involved in the corporation's misconduct, including officers and directors. According to a spokesman for the Justice Department, "To ensure that companies understand the importance of this, the Fraud Section now requires that cooperating companies confirm to us that they have, in fact, turned over all non-privileged information about individuals." Corporations must now name names to receive cooperation credit. The intent of the certification requirement is clear:

[c]ompanies cannot just disclose facts relating to general corporate misconduct and withhold facts about the individuals involved. Internal investigations cannot end with a conclusion of corporate liability, while stopping short of identifying those who committed the underlying conduct.

The current climate of individual accountability for corporate misconduct requires business leaders to respond more proactively, and thoughtfully, to allegations or complaints of impropriety. Here are but a few additional considerations that must be weighed:

- Corporate boards and executives must carefully consider the impact of the department's increased focus when investigating allegations or complaints of impropriety.
- The committee directing an internal investigation must structure the investigation to ensure that identities and specific facts may be shared with the department and must do so without creating a waiver of the attorney-client privilege.
- The corporation must provide all nonprivileged information about any impropriety and the identity of individuals involved in the conduct.

The department's new policies represent a significant culture shift. The board of directors, audit committee or other special committee, as well as the C-Suite, must now contemplate questions of attorney-client privilege, conflicts of interest and fiduciary responsibilities to the corporation. It is not certain that the department's new certification process puts officers and key employees at odds with the interests of the corporation, but the possibility of divergent interests must now be considered proactively at the outset of any interview in order to best protect both the corporation and its key employees. Officers and key employees must evaluate and balance the impact of cooperating with an internal investigation. They must understand the duties they owe to the corporation and its shareholders and assess the exposure created by their involvement being shared with the DOJ.

Certainly, had the investigation of wrongdoing in connection with the 2008 Financial Crisis been conducted with the priorities outlined in the Yates Memo, Wall Street would have been compelled to turn over the names of the individual executives and key employees involved in creating, valuing, trading, and profiting from the securities at the heart of the crisis. Many of those individuals would have faced rigorous scrutiny and criminal charges.

Everyone supports individual accountability in the instances of a rogue employee embezzling funds or defrauding a customer for his own benefit to the detriment of the corporation. This policy applies equally to the collective efforts of the corporation to meet market expectations, improve poor performance, keep investors feeling good about their investments, etc. A corporation and its shareholders also have an interest in an efficient, cooperative resolution with the Department of Justice. Corporations must now move quickly, but deliberately, to address concerns about possible wrongdoing and protect themselves, their shareholders, as well as officers and key employees. ■

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