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Conducting Internal Investigations

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INTRODUCTION

In the wake of recent corporate scandals, the financial crisis and the enactment of tougher corporate accountability standards under the Sarbanes-Oxley Act of 2002 ("SOX")[1] and the Dodd-Frank Act,[2] internal investigations have become an important exercise of good corporate governance. Internal investigations can be initiated for a variety of reasons, including allegations of significant corporate misconduct that could violate federal or state law, a complaint from an employee, ethical lapses or wrongdoings by a competitor.

Indeed, under certain circumstances, an internal investigation may be required by law or corporate policy or, at a minimum, strongly warranted to assist the corporation in staving off regulatory action, limiting significant civil monetary penalties, or avoiding suspension and bar orders. A thorough and credible internal investigation may help determine, and often improve, the course of regulatory and criminal investigations, as well as shareholder and third-party litigation. Conversely, a poorly conducted investigation can place a corporation, and its directors and officers, in a worse position than they would have been in the absence of such an investigation.

Internal investigations may take many forms, depending upon the nature of the conduct at issue and the scope of the investigation. If the suspected misconduct is limited and discrete, an internal investigation may be conducted by the corporation's in-house counsel, compliance department or its internal audit department. However, if the suspected misconduct is significant, or involves senior management or the board of directors, it likely should be conducted by outside counsel.

While every internal investigation has unique characteristics, to be most effective they should be timely, thorough, accurate, fair, objective and credible. If an internal investigation does not meet all of these goals, it likely will be ineffective. Credibility is key, and as the seriousness of the conduct at issue increases, so should the independence of counsel conducting the investigation.

This article discusses some of the considerations that are important to the decision whether to conduct an internal investigation, the benefits and pitfalls of such investigations, and the techniques for properly steering the course and conduct of the investigation.

Internal investigations may take many forms, depending upon the nature of the conduct at issue and the scope of the investigation.

[1] Pub. L. No. 107-204, 116 Stat. 745 (2002).

[2] Pub. L. No. 111-203 (2010).

DECIDING WHETHER TO INITIATE AN INTERNAL INVESTIGATION

A decision whether to initiate an internal investigation is sometimes extremely difficult to make and may require significant analysis. It is an important decision as once the decision to initiate an internal investigation is made, it likely cannot be reversed. Conversely, great harm can result if a regulator believes that an internal investigation should have been done and the decision was made not to conduct one.

In deciding whether to conduct an internal investigation, a company should take into consideration a number of factors including: (a) whether such an investigation is required by any law, regulation or corporate policy; (b) the scope and severity of the alleged misconduct and potential violations of law and regulation; (c) potential or actual interest or litigation by civil regulators, criminal authorities, and third parties; and (d) the benefits and risks to the corporation and/or its officers, directors and employees of such an investigation. Depending on the nature of the misconduct at issue, an internal investigation can consume tremendous resources, at great cost to the company, and potentially expose the company and its officers to greater liability by setting forth a blueprint for regulatory and private actions. The cost of inaction to a company, however, could swiftly outweigh any expense and litigation risk associated with a properly conducted investigation. Failure to complete the investigation in a credible, timely and thorough manner could also be viewed as an attempt to cover-up wrongdoing.[3]

By the same token, a company's basis for conducting an investigation will determine the manner in which the investigation is conducted, and how the results of the investigation will be reported and addressed. Internal investigations can be used as a means for identifying and remedying misconduct within a company, as well as a defensive mechanism for addressing regulatory and prosecutorial investigations and private claims.

STATUTORY AND REGULATORY OBLIGATION TO INVESTIGATE

The use of internal investigations as a defensive mechanism has its roots in the SEC's "voluntary disclosure program" of the 1970s, which arose in response to widespread allegations of corruption and bribery, and led to the enactment of the Foreign Corrupt Practices Act of 1977 ("FCPA"). Under that program, companies established special committees of their boards of directors to retain outside counsel in order to conduct internal investigations, prepare reports of the findings, and disclose the reports from the investigation to the SEC.[4] In the following years, federal and state regulators continued to promote voluntary disclosure programs as an enforcement mechanism.[5] These programs rewarded companies who responded to reports of misconduct by initiating internal investigations and disclosing their results to regulators, with reductions in sanctions or even complete avoidance of enforcement action.

Nevertheless, corporations and regulated entities may also have legal obligations to conduct an independent investigation depending on the circumstances of the alleged conduct. For instance, SOX requires, among other things, corporations to establish audit committees with responsibility for developing procedures to receive, retain and investigate complaints of financial fraud involving auditing, accounting or internal controls issues.[6] The chief executive officer and chief financial officer are required to certify that the company's public filings fairly present, in all material respects, the company's

[3] *See SEC v. Endocare, Inc.*, Litig. Release No. 19772, 2006 SEC LEXIS 1658 (July 25, 2006) (corporation sanctioned with $750,000 fine for accounting fraud and for making misleading public statements about the results of an internal investigation).

[4] *See generally SENATE COMM. ON BANKING, HOUSING, AND URBAN AFFAIRS, 94TH CONG., 2D SESS., REPORT OF THE SECURITIES AND EXCHANGE COMMISSION ON QUESTIONABLE AND ILLEGAL CORPORATE PAYMENTS AND PRACTICES 6-13* (Comm. Print 1976). More than 400 U.S. corporations, including more than 100 Fortune 500 companies, participated in the program. See Sarah Helene Duggin, *Internal Corporate Investigations: Legal Ethics, Professionalism and the Employee Interview*, 2003 COLUM. BUS. L. REV. 859, 873 (2003).

[5] These include the Department of Justice's Antitrust Division Voluntary Disclosure Program and Corporate Leniency Policy, the joint Departments of Justice and Defense Voluntary Disclosure Program; and the Department of Health and Human Services' Operation Restore Trust.

[6] SOX § 301, 15 U.S.C. § 78j-1 (2006) (also requiring that audit committees be empowered to retain independent counsel or experts to fulfill such duties).

Financial services firms such as broker-dealers and investment advisers who are regulated by SROs may have obligations to self-report violations of law and SRO rules to the regulators.

financial condition and results of operations.[7] In addition, attorneys appearing or practicing before the SEC must report "up the ladder" (i.e. to senior management and/or the company's board) certain material violations of securities laws or breaches of fiduciary duties, creating additional pressure on management to act.[8]

Financial services firms such as broker-dealers and investment advisers who are regulated by SROs may have obligations to self-report violations of law and SRO rules to the regulators. In derivative lawsuits brought on behalf of corporations by shareholders, corporations may be required by courts to conduct an independent investigation of alleged misconduct, often by establishing a special litigation committee of the board of directors. Indeed, such an investigation may be warranted in order for corporate directors to satisfy their duty of care.[9] Moreover, in situations involving potential fraud or material misstatement in a company's financial statements, an internal investigation may be a prerequisite for the company's outside auditors to continue to perform the company's audit or, where new auditors are necessitated, for successor auditors to agree to undertake the audit engagement.[10]

Conducting a thorough internal investigation can be critical in responding to whistleblower complaints in light of the SEC's Whistleblower Program established pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act.[11] The SEC does not require that a company conduct its own investigation after receiving an internal tip, but encourages whistleblowers to first report their complaint internally before approaching the SEC. The SEC factors whether and how such internal reporting occurred and the company's response in determining whether to bring an enforcement action against the company and, if so, whether to award money to the whistleblower. An award could range between 10 and 30 percent of the monetary sanctions collected in an SEC action and any related actions. To that end, the SEC will assess whether the whistleblower: (i) "participated in internal compliance systems"[12]; (ii) "unreasonably delayed reporting the securities violations"[13]; or (iii) "undermined the integrity"of the company's internal compliance systems.[14] While the process for determining awards is not outwardly transparent, the SEC has brought enforcement actions where the entity failed to investigate and take corrective measures or responded by retaliating against the reporting employee.[15] Conducting a thorough internal investigation may help a company defend itself in an enforcement investigation by demonstrating that the alleged violations were investigated and, if found reliable, promptly and effectively remedied.

EXTENT OF MISCONDUCT AND POTENTIAL VIOLATIONS

Not all reports of misconduct at a company will necessitate an internal investigation conducted by outside counsel under the aegis of a board committee. Generally, where the alleged misconduct involves an individual employee and does not implicate potential violations of federal or state law, in-house counsel, often in conjunction with a company's internal audit department, can investigate the allegations and recommend to management appropriate remedial and personnel actions. However, an internal investigation conducted by outside counsel under board supervision should be strongly considered where the misconduct is widespread or may involve corporate officers or directors, affect the company's governance, potentially violate federal or state law, or corporate policy, or subject the company to regulatory or prosecutorial investigation and possible enforcement action.

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[7] SOX § 302, 18 U.S.C. § 1350(b) (2006).

[8] SOX § 307, 15 U.S.C. § 7245 (2006).

[9] *See generally In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959, 970 (Del. Ch. 1996) (a director has "a duty to attempt in good faith to assure that a corporate information and reporting system . . . is adequate, [and] exists . . . .").

[10] *See generally* Codification of Auditing Standards and Procedures, Statement on Auditing Standards No. 1, § 110.02 (Am. Inst. of Certified Pub. Accountants 1972) ("The auditor has a responsibility to . . . obtain reasonable assurance about whether the financial statements are free of material misstatement"); Illegal Acts by Clients, Statement on Auditing Standards No. 54, § 317.10 (Am. Inst. of Certified Pub. Accountants 1988) (requiring that "[w]hen the auditor becomes aware of information concerning a possible illegal act, the auditor should obtain an understanding of the nature of the act, the circumstances in which it occurred, and sufficient other information to evaluate the effect on the financial statements.").

[11] 15 U.S.C. § 78u-6.

[12] 17 C.F.R.§ 240.21F-6(a)(4) (2011).

[13] 17 C.F.R. § 240.21F-6(b)(2) (2011).

[14] 17 C.F.R. § 240.21F-6(b)(3) (2011).

[15] *See e.g., In the Matter of Paradigm Capital Mgmt, Inc. and Candace King Weir*, Admin. Proc. Release No. 3-15930, 2014 SEC LEXIS 2104 (June 16, 2014) (SEC's first Dodd-Frank anti-retaliation enforcement action imposing $2.2 million in disgorgement and penalties against investment adviser for violating Section 206(3) of the Investment Advisers Act of 1940 by engaging in prohibited principal transactions, and Section 21F(h) of the Securities Exchange Act of 1934 by retaliating against whistleblower).

RESPONDING TO REGULATORY OR ENFORCEMENT INQUIRIES

If a company is aware that it is under investigation or the subject of complaint to a regulatory or law enforcement entity, the company should consider initiating its own investigation. To do so will set an important tone with the regulators by demonstrating that the company is diligently and independently seeking to discover the facts and evidence, and take appropriate steps to expose and remedy the misconduct. It will also enable the company to better understand the veracity of the allegations, the extent of any misconduct and any defenses the company may have. Proactive steps to investigate not only assist the regulators in quickly gathering the facts and any evidence, but also allow the investigated company to stay several steps ahead of the regulators and focus its energies on crafting appropriate corrective action that may be used to persuade regulators that the misconduct has been thoroughly investigated and remedied.

BENEFITS AND PITFALLS OF AN INTERNAL INVESTIGATION

INTERNAL INVESTIGATIONS AS A FORM OF COOPERATION

Internal investigations have grown in importance amidst heightened scrutiny of corporate conduct and an emphasis on a culture of corporate compliance and responsibility. When considering whether to impose civil or criminal penalties, both the SEC and DOJ will consider a corporation's willingness to undertake and voluntarily disclose the results of a properly conducted internal investigation.[16] The government welcomes internal investigations and self-disclosure in part because they conserve enforcement resources.[17] Such investigations are useful mechanisms for assisting a company in identifying personnel who should be terminated, and deficient systems and procedures that need to be improved.

In some cases, undertaking an internal investigation, sharing the results of the investigation with regulators and taking remedial steps may enable a company to avoid charges against the corporation even as individuals become the targets of an investigation or litigation.[18] In other cases, such investigation may reduce the amount of civil penalties imposed by the SEC,[19] or eliminate any civil money penalty.[20] In the case of criminal investigations, where a company may be held criminally liable for its employees' illegal conduct,[21] tangible efforts to cooperate with authorities, including through the conduct of an independent investigation and disclosure of its results, may garner avoidance or deferment of criminal prosecution.[22] By contrast, failure to investigate reported wrongdoing or to respond effectively to "red flags" can bolster the government's case for imposing a civil penalty.[23]

Moreover, an internal investigation may enable the company to identify more quickly information that will likely be obtained by the government, and thereby enable the company to respond more effectively to the government's investigation. An internal investigation will further assist the company in gathering information, fashioning defenses and crafting a remedy for the misconduct. Internal investigations also enable a company to assess the level of potential wrongdoing that can inform the decision whether to settle and, if so, to determine an appropriate settlement threshold. At times, a company may be able to forestall or limit the scope of a government investigation by demonstrating that the company is independently and reliably gathering facts and evidence that can be assessed by regulators with limited resources of their own. Alternatively, an internal investigation may help a company persuade the government or law enforcement entities to focus the investigation on particular individuals responsible for the misconduct. Finally, internal investigations enable companies more effectively to assist board members, officers and employees in preparing for and giving testimony.

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[16] *See, e.g.*, Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934 and Commission Statement on the Relationship of Cooperation to Agency Enforcement Decisions, Exchange Act Release No. 44969, 2001 SEC LEXIS 2210, at *1-2 (Oct. 23, 2001) ("Seaboard Report") (factors in the decision to forego an enforcement action include: hiring outside counsel to conduct a thorough inquiry; dismissing employees that committed wrongdoing; producing the details of its internal investigation to the SEC, including notes and transcripts; and, choosing not to invoke the attorney-client privilege, work product protection, or other privileges).

[17] Seaboard Report at *3.

[18] See Seaboard Report at *1-3; (declining to charge corporation on the basis of its internal investigation and waiver of privileges to disclose results of the investigation); see also *SEC v. Faria*, Litig. Release No. 19656, 2006 SEC LEXIS 844, at *3-4 (Apr. 13, 2006) (company avoids civil fraud charges by SEC because of its "extensive cooperation . . . [which] consisted of prompt self-reporting, an independent internal investigation, sharing the results of that investigation with the government, disciplining responsible wrongdoers, and implementing new controls designed to prevent the recurrence of the improper conduct."); *SEC v. Dooley, Litig.* Release No. 18896, 2004 SEC LEXIS 2205, at *6 (Sept. 23, 2004); *SEC v. Giesecke*, Litig. Release No. 17745, 2002 SEC LEXIS 2423, at *8-9 (Sept. 25, 2002).

[19] *See, e.g., SEC v. Am. Int'l Group*, Litig. Release No. 19560, 2006 SEC LEXIS 277, at *5-6 (Feb. 9, 2006) ("complete cooperation" defined by SEC as the company undertaking an internal investigation, "promptly provid[ing] information regarding any relevant facts and documents uncovered in its internal review [and] provid[ing] the staff with regular updates on the status of the internal review"). See also *Canadian Imperial Holdings*, Securities Act Release No. 8592, 2005 SEC LEXIS 1773, at *37-38 (July 20, 2005); *Banc of Am. Capital Mgmt.*, Securities Act Release No. 8538, 2005 SEC LEXIS 291, at *59 (Feb. 9, 2005); *Monsanto Co.*, Exchange Act Release No. 50978, 2005 SEC LEXIS 10, at *16-17 (Jan. 6, 2005); *Alliance Capital Mgmt.*, Advisors Act Release No. 2205, 2003 SEC LEXIS 2997, at *30 (Dec. 18, 2003).

[20] *See, e.g., ING Groep N.V.*, Securities Act Release No. 8594, 2005 SEC LEXIS 1880, at *6-7 (July 26, 2005); *CyberGuard Corp.*, Exchange Act Release No. 45362, 2002 SEC LEXIS 236, at *17 (Jan. 30, 2002).

[21] *See, e.g., United States v. Inv. Enter., Inc.*, 10 F.3d 263, 266 (5th Cir. 1993) (a corporation can be held liable for the unlawful acts of its agents if their conduct is within scope of their actual or apparent authority). See generally Joseph S. Hall, *Corporate Criminal Liability*, 35 AM. CRIM. L. REV. 549 (1998).

[22] *See, e.g., Deferred Prosecution Agreement, United States v. Computer Assocs. Int'l, Inc.*, Cr. No. 04-837 (ILG) (E.D.N.Y. 2004), available at http://www.usdoj.gov/dag/cftf/chargingdocs/compassocagreement.pdf; Deferred Prosecution Agreement between Bristol-Myers Squibb and the United States Attorney for the District of New Jersey, available at http://www.usdoj.gov/usao/nj/press/files/pdffiles/deferredpros.pdf. See generally McNulty Memorandum at § VII.B.1.

[23] *See United States v. Phelps Dodge Indus., Inc.*, 589 F. Supp. 1340, 1363 (S.D.N.Y. 1984) (observing that a demonstration of good or bad faith is an important factor in determining the appropriate level of civil monetary penalty, and noting that the company "responded with insufficient vigor to tangible indications of [an employee's] illegal conduct").

IDENTIFYING REMEDIAL STEPS AND PREVENTING FUTURE MISCONDUCT

Irrespective of any impact on potential civil or criminal liability, there are sound business reasons to investigate reports of wrongdoing. Failure to investigate may send the message that the company does not take wrongdoing seriously. By contrast, quick action in investigating and remedying misconduct will help the company in showing employees that it expects them to abide by established codes of conduct and demonstrating to the government that the company is a good corporate citizen.

THE RISKS OF INVESTIGATION

While the benefits of conducting an internal investigation are substantial given the post-Enron regulatory environment, there are risks that should be considered and, where possible, minimized. The costs, expenses and disruptions to the company associated with such investigations can be significant, depending on the magnitude of the conduct at issue, and how the investigation will be staffed and conducted.

Beyond such issues, an internal investigation will result in the development of a factual record that may serve as a blueprint to regulators and private litigants seeking to assert claims against the company and its officers and directors. These disclosures to the government and potential third party claimants may include not only the identity of any malfeasants, but also information regarding relevant witnesses and documents, witness statements and interview memoranda, as well as any written report of the investigation. The extent of such a blueprint may largely depend on whether the company waives its attorney-client or attorney work product privileges to disclose the investigation's findings. Nevertheless, at a minimum, the facts and evidence identified in an internal investigation may be discoverable by third parties who could in turn be advantaged by the prior development of a readily accessible record of the wrongdoing.

An internal investigation may also result in discovery of misconduct beyond the scope of the initial allegations of wrongdoing. The credibility of an investigation may suffer if all appropriate and relevant leads are not pursued. To the extent apparently unrelated misconduct is identified, a thorough analysis should be done to determine whether it should be included in the scope of the investigation.

There are significant limitations to an internal investigation that should be considered. The success of any internal investigation may be dependent on the extent of cooperation given by current and former employees, as well as third party witnesses. Given that subpoena power is not present in internal investigations, cooperation cannot be compelled by law. Moreover, confidentiality and business considerations may limit investigating counsel from contacting and interviewing third-party witnesses. However, the company may be able to link cooperation by current and former employees to continued employment and/or indemnification for legal fees and expenses, assuming there are no contracted or legal rights to indemnification.

While the benefits of conducting an internal investigation are substantial given the post-Enron regulatory environment, there are risks that should be considered and, where possible, minimized.

THE INVESTIGATION PROCESS

ESTABLISHING THE IDENTITY OF THE CLIENT AND THE SCOPE OF THE INVESTIGATION

Once the decision to undertake an internal investigation has been made, the next step is to determine precisely on whose behalf the investigation is being conducted, as well as its scope. Those decisions should be memorialized in writing, such as in the form of a detailed engagement letter setting forth the agreement to retain outside counsel to conduct the investigation.

In many cases, the investigation will be conducted by management of the company. In other situations, the investigation will be controlled by the company's Board of Directors, a standing committee of the board (such as the audit committee) or a special investigatory committee formed to assume responsibility for the investigation. Such committees may be required in the context of derivative lawsuits, or warranted where senior officers or even board members are subjects of the investigation. A special committee can help protect the investigation from being controlled or unduly influenced by individuals with conflicted interests in the outcome of the investigation.

The scope and purpose of the investigation should be specifically identified. At the same time, an investigation should not be so narrowly circumscribed as to undermine inquiries that may well serve the purpose of an internal investigation even if they are not directly related to the initial suspected misconduct. Because investigations are, by their very nature, generally initiated at any early stage of a client's knowledge of the extent of misconduct, it may be necessary for counsel to re-evaluate the investigation's scope throughout the course of an investigation.

PREVENTING COMMON PITFALLS

Preservation of Evidence and Records

Failure to preserve relevant documents immediately after an investigation is initiated can seriously hamper an internal investigation. At worst, it can result in charges of obstruction of justice where government investigations have been initiated or are anticipated.[24] In large investigations, a document preservation notice should be issued to the company's relevant employees informing them of the investigation, and requiring that they not destroy any documents potentially relevant to the subject matter of the investigation. Identifying relevant employees may be difficult as the scope of the conduct to be investigated may not be known at the outset. The notice should give sufficient detail so that employees will know what documents need to be preserved, but not so much that it gives a roadmap of the investigation. Further, all automated data destruction or deletion processes should cease. Particular care should be taken to preserve all electronic communications and documents, including images of relevant employee hard drives, laptops and email devices or PDAs, including even, if possible, employees' personal computers, back-up tapes, and PDAs.

Preserving Privileges

Both the investigative record and the documents and data created in the course of the investigation are typically protected by the attorney-client privilege, the work product doctrine, or both. These protections are critical to maintaining the maximum control over the results and underlying documentation of the investigation. While there are situations in which the company will choose on its own to waive some or all of the protections on the investigatory record,[25] the company may not reach that decision at the beginning of the investigation. Failure to maintain the privilege may leave some of the company's most sensitive information, including the findings and report of the investigation, in the hands of regulators, litigation opponents, and even competitors.

Although the corporation may choose to disclose the results of an investigation, management and counsel should take every precaution to ensure that disclosure remains a viable option and not a forced circumstance based upon failure to protect privileges during the course of the investigation. All personnel involved in the investigatory process must be strictly warned about the importance of confidentiality

[24] SOX includes new penalties for any person who "knowingly alters, destroys, mutilates, conceals, covers up, falsifies or makes a false entry in any record, document, or tangible object with the intent to impede, obstruct, or influence" any government investigation. 18 U.S.C. § 1519 (2006).

[25] *See infra* Section D.2.

and the need to avoid any disclosures about the nature or conduct of the investigation, except as deemed necessary by counsel. The Supreme Court has made it clear that when internal investigations are undertaken by in-house counsel, communications between counsel and employees concerning matters within the scope of the employees' corporate duties and undertaken for the purpose of securing legal advice are protected by the attorney-client privilege.[26] Since the landmark 1981 Supreme Court decision in *Upjohn*, courts have generally held that counsel's efforts to uncover facts as part of an internal investigation are sufficiently legal in nature to warrant application of the attorney-client privilege.[27] Management should take particular notice that preliminary investigations conducted by management will not receive the benefits of privilege protection, even if the company subsequently retains counsel to conduct a full investigation.[28] It will therefore generally be advisable that company management elicit the oversight (rather than mere peripheral involvement) of attorneys at the earliest possible stage of any investigatory effort.

The protections of the attorney-client privilege apply to employee communications with counsel if:

(1) the communication was made for the purpose of securing legal advice;

(2 the employee making the communication did so at the direction of his corporate superior;

(3) the superior made the request so that the corporation could secure legal advice;

(4) the subject matter of the communication is within the scope of the employee's corporate duties; and

(5) the communication is not disseminated beyond those persons who, because of the corporate structure, need to know its contents.[29]

Consequently, counsel conducting internal investigations should be careful to document that the investigation is being conducted at the client's request and is undertaken for the purpose of providing legal advice.[30] That fact should be documented by the engagement letter and should be repeated wherever appropriate, including during interviews and in any written summaries of interviews with employees. Counsel should also ensure that management directs employees to cooperate with the investigation. Any documentation of interviews with employees should specify that the information provided falls within the scope of employment and aids the investigation.

Although the attorney-client privilege will not attach absent the involvement of an attorney, the privilege may extend to non-attorney personnel who are carrying out investigatory tasks as agents of the attorney(s) with oversight over the investigation.[31] The services of knowledgeable employees or experts may thus be used to assist with the investigation provided proper steps have been taken to document that the investigatory efforts are being carried out at the behest of counsel in performance of legal services. Additionally, the investigators may also retain experts to assist the attorneys with technical issues.[32] Any privileges belonging to the internal investigation team can be better protected by clearly establishing that the experts were retained directly by counsel.

Courts distinguish between "factual" and "opinion" work product. Factual work product refers to documents that contain information essentially factual in nature, while opinion work product refers to documents containing mental impressions, legal theories or legal opinion and analysis. As specified by the Federal Rules of Civil Procedure, while factual work product is technically covered by the work product doctrine, it may be discoverable upon a showing of "substantial need" for the information.[33] Opinion work product, by contrast, enjoys virtually absolute protection.[34] Attorneys can maximize the potential for work product protection by integrating legal analysis into documents rather than merely recounting facts. For instance, if counsel chooses to prepare a record of an employee interview, the record should not be a substantially verbatim transcript or summary of the interview, but should instead incorporate the mental impressions of counsel about the substance of the interview, and should prominently state that it does so on the interview memorandum.

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[26] *Upjohn Co. v. United States*, 449 U.S. 383, 394 (1981).

[27] *See, e.g., In re Allen*, 106 F.3d 582, 602 (4th Cir. 1997), cert. denied, 522 U.S. 1047 (1998). *But see In re Royal Ahold N.V. Sec. & ERISA Litig.*, 230 F.R.D. 433, 435 (D. Md. 2005) (finding that work product protection did not apply to interview memoranda from internal investigation when investigation "would have been undertaken even without the prospect of preparing a defense to a civil suit"); *In re Kidder Peabody Sec. Litig.*, 168 F.R.D. 459, 465 (S.D.N.Y. 1996); *In re Leslie Fay Cos., Sec. Litig.*, 161 F.R.D. 274, 281 (S.D.N.Y. 1995) (rejecting work product protection for Audit Committee investigation because it was "not conducted primarily in anticipation of litigation," but instead was for business reasons) (emphasis added).

[28] *See, e.g., In re Grand Jury Subpoena*, 599 F.2d 504, 510 (2d Cir. 1979).

[29] *Diversified Indus., Inc. v. Meredith*, 572 F.2d 596, 609 (8th Cir. 1978); *see also Harper & Row Publishers, Inc. v. Decker*, 423 F.2d 487, 491-92 (7th Cir. 1970), aff'd, 400 U.S. 348 (1971), and reh'g denied, 401 U.S. 950 (1971).

[30] Communications between corporate employees and counsel during an internal investigation are privileged as long as "providing legal advice was one of the significant purposes of the internal investigation." *In re Kellogg Brown & Root, Inc.*, 756 F.3d 754, 758, 760 (D.C. Cir. 2014) (holding that the privilege was not defeated where the investigation was initiated to satisfy a regulatory requirement or corporate policy such as federal defense contractor regulations).

[31] See, e.g., *Carter v. Cornell Univ.*, 173 F.R.D. 92, 95 (S.D.N.Y. 1997), aff'd, No. 97-9180, 1998 U.S. App. LEXIS 18807 (2d Cir. July 9, 1998); *United States v. Davis*, 131 F.R.D. 391, 398 (S.D.N.Y. 1990).

[32] Cases involving accounting fraud lend themselves particularly well to the retention of accounting experts to assist the investigators with accounting questions.

[33] Fed. R. Civ. P. 26(b)(3).

[34] *Id., see also* Upjohn, 449 U.S. at 401.

The biggest hurdle to a work product claim over documents prepared during the course of an investigation is typically the "anticipation of litigation" requirement. Generally, there must be an identifiable prospect of litigation to warrant work product protection. Some courts have adopted a restrictive "predominating purpose" test, according to which a document must have been created or prepared primarily to assist in pending or impending litigation.[35] However, a majority of courts have adopted a more flexible "because of" test, holding that documents are prepared in anticipation of litigation when they were prepared "because of" the prospect of litigation.[36] Courts adopting this test have generally required that the expectation of litigation be objectively reasonable, as well as guided by a subjective belief.[37] Because every investigation is unique, the validity of a work product claim will depend upon the circumstances. A work product claim will be strongest when an investigation is opened up in response to a government inquiry. Several courts have held that investigations by regulatory authorities present more than simply a remote possibility of litigation.[38] A work product claim will be more tenuous when a corporation undertakes an investigation in response to internal reports of potential wrongdoing. Nevertheless, a corporation may strengthen a work product claim if it can prove that it was responding to specific claims, and determined that an internal investigation would be helpful in responding to anticipated litigation or regulatory investigations. Consequently, documents identifying the scope of the investigation or reporting the results of the investigation should record, where appropriate, that the investigation was undertaken to provide legal advice in anticipation of litigation.

There should be recognition at the outset of any investigation that certain materials prepared during the course of the investigation may eventually be subject to disclosure to law enforcement authorities or other third parties. Consequently, counsel should instruct all personnel participating in the investigation that documents should only be created as deemed necessary, and in the manner prescribed by counsel.

Although final decisions about whether and how to report the results of an investigation may be left to the end of the investigation, early consideration should be given to the likely final product. Anticipating the nature of the final product

There should be recognition at the outset of any investigation that certain materials prepared during the course of the investigation may eventually be subject to disclosure to law enforcement authorities or other third parties

can help ensure that the documentary and oral information necessary to prepare the final report is obtained during the course of the investigation.

Several steps can be taken to prevent the inadvertent waiver of the privilege. First, and most simply, all privileged and work-product documents should be clearly labeled "Confidential," and should note which protection applies. This will help to demonstrate the intent to maintain the confidentiality of the documents. Further, any disclosures, even to the government, should be subject to a "non-disclosure agreement" (or something similar), restricting the right of the receiving party to share the information with third parties. Such agreements may be seen as evidence of the continuing efforts to maintain some degree of confidentiality and may be helpful in limiting the scope of any waiver that has been affected by the disclosure.

To the extent that information is shared with other parties, such as current or former employees, care must be taken not to inadvertently effect a waiver. A "joint defense" or "common interest" agreement may be formed between parties as "part of an ongoing and joint effort to set up a common defense strategy,"[39] and will generally create a "joint defense privilege" that acts as an exception to the rule that disclosure to a third party will act as a waiver of privileged communications.[40] Though such an agreement may be found to have been created orally, the burden of establishing the existence of the joint defense privilege will fall to the party claiming it.[41] Therefore, it may be preferable to obtain a written "joint defense agreement" from any party with whom information is shared. As a general rule, courts have found that joint defense privileges apply as long as the parties have some common interests, even if their interests

[35] *See, e.g., United States v. The El Paso Co.*, 682 F.2d 530, 542-43 (5th Cir. 1985), cert. denied, 466 U.S. 944 (1984); *Heffron v. Dist. Court of Okla. County*, 77 P.3d 1069, 1079 (Okla. 2003); *Ex parte Cryer*, 814 So. 2d 239, 247 (Ala. 2001).

[36] *See, e.g., United States v. Roxworthy*, 457 F.3d 590, 593 (6th Cir. 2006); *United States v. Torf (In re Grand Jury Subpoena)*, 357 F.3d 900, 907 (9th Cir. 2003); *Maine v. United States DOI*, 298 F.3d 60, 68 (1st Cir. 2002); *United States v. Adlman*, 134 F.3d 1194, 1202 (2d Cir. 1998); *United States v. Naegele*, 468 F. Supp. 2d 165, 173 (D.D.C. 2007) *Lawrence E. Jaffe Pension Plan v. Household Int'l, Inc.*, 237 F.R.D. 176, 181 (N.D. Ill. 2006).

[37] *Roxworthy*, 457 F.3d at 593-94.

[38] *See, e.g, Adlman*, 134 F.3d at 1202 (extending a work product claim to a document created with the mixed purpose of preparing for possible litigation and aiding in a business decision); *Martin v. Bally's Park Place Hotel & Casino*, 983 F.2d 1252, 1260-61 (3d Cir. 1993).

[39] *In re Grand Jury Subpoena*, 274 F.3d 563, 572 (1st Cir. 2001) (citation omitted).

[40] The common elements for establishing the existence of a joint defense privilege are that: (1) the communications were made in the course of a joint defense effort; (2) the statements were made in furtherance of that effort; and (3) the privilege has not been waived. *See, e.g., United States v. LeCroy*, 348 F. Supp. 2d 375, 381 (E.D. Pa. 2004).

[41] *See United States v. Weissman*, 195 F.3d. 96, 99 (2d Cir. 1999); *LeCroy*, 348 F. Supp. 2d at 381.

are not identical,[42] but have rejected such a privilege claim in instances where the parties' interests are so divergent as to make them effectively adversaries.[43] Accordingly, a careful analysis should be performed of the extent to which parties' interests do or may potentially diverge prior to the sharing of information between these parties.

Further, because internal investigations can be international in scope, it is important to note that attorney-client privilege varies from country to country. For example, while every European Union member state has at least some form of attorney-client privilege, the extent of this protection varies significantly from country to country.[44] Additionally, at least for enforcement actions taken by the European Commission, the European Court of Justice has ruled that "legal professional privilege" does not apply to communications between the corporation and its in-house counsel because, in the eyes of the court, these attorneys are not sufficiently independent of the client.[45] For this reason, companies facing a government enforcement action or considering conducting an internal investigation should understand the extent to which attorney-client privilege applies in each relevant country and should consider hiring outside counsel to protect legal communications.

STAFFING THE INVESTIGATION

Retaining Outside Counsel

There are obvious benefits to relying upon in-house counsel to perform an internal investigation.[46] Aside from the costs involved in retaining outside counsel, in-house counsel are more likely than outside counsel to understand a company's general business operations and be most familiar with relevant personnel. Management may also feel more comfortable with having insiders investigating potential wrongdoing.

There are, however, more compelling reasons to retain outside counsel to perform the investigation. At a minimum, the retention of outside counsel gives greater assurance that an investigation is perceived as independent. This can be very significant to the DOJ, SEC, and other regulators. Additionally, while the attorney-client privilege may be extended to investigations undertaken by in-house counsel, outside counsel generally have an easier task in proving that they are acting in a legal rather than business capacity. Further, outside counsel may have developed expertise in the conduct of internal investigations, including investigatory techniques, protecting privileges, knowledge of applicable law, working with enforcement authorities and crafting reports prepared for disclosure. The investigated conduct may also require counsel who specializes in particular substantive areas of the law, such as compliance with federal securities laws, or government procurement statutes. Outside counsel will often also be better equipped to devote the requisite resources to an investigation. It is generally better to complete an investigation as quickly as possible, typically in a matter of weeks or months. Investigations may require analysis of hundreds of thousands of documents, dozens of employee interviews and the near full-time participation of dozens of attorneys and support staff. In some cases, the advice of in-house counsel may itself be under investigation, or may become a subject of investigation, resulting in a conflict of interest if they are responsible for the investigation. Lastly, any enforcement authorities are more likely to perceive outside counsel as independent.

If outside counsel is engaged to conduct an investigation, a further decision is whether to use outside counsel with pre-existing relationships to the company. Outside counsel with longstanding relationships to the company will have insights into the company's general operations and personnel that could prove invaluable in undertaking an investigation, as well as effective working relationships with in-house counsel. However, the greater the prior relationship between the company and counsel, the greater the risk to the independence and objectivity of the investigation.

Establishing Reporting Lines of Authority and Supervision

Outside counsel conducting an internal investigation may have to coordinate new lines of supervision and authority. Depending on the nature of alleged wrongdoing, senior management or even the general counsel's office itself may be implicated in the misconduct. In such situations the investigatory team should not "report" through the normal chain of command (i.e., to the general counsel). Instead, the establishment of a special committee or other committee

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[42] *See United States v. Weissman*, No. 5194 Cr. 760, 1996 U.S. Dist. LEXIS 19066, at *33 (S.D.N.Y. 1996) (holding "that a joint defense may be made by somewhat unsteady bedfellows does not in itself negate the existence or viability of the joint defense") (citing *In re Grand Jury Subpoena Duces Tecum*, 406 F. Supp. 381 (S.D.N.Y. 1975)).

[43] *See, e.g., McNally Tunneling Corp. v. City of Evanston*, No. 00 C 6979, 2001 U.S. Dist. LEXIS 17090, at *9 (N.D. Ill. Oct 18, 2001) (common interest privilege not available as to communications concerning matter in which parties were adverse).

[44] Laurel S. Terry, Introductory Note to the Court of Justice of the European Union: The *Axzo Nobel* EU Attorney-Client Privilege Case, 50 I.L.M. 1 (2011) ("[E]ach EU Member State has its own set of rules or case-law governing the confidentiality or privileged nature of communications between clients and their lawyers . . . . Although EU Member States differ with respect to the nature, scope, and source of the confidentiality protection, all EU Member States offer some sort of protections.").

[45] Case C-550/07 P, *Akzo Nobel Chemicals and Akcros Chemicals Ltd. v. European Commission* [2010] I-08301, Opinion of AG Kokott.

[46] The attorney-client privilege and work product may also attach itself to investigations undertaken by in-house counsel. *United States v. United Shoe Mach. Corp.*, 89 F. Supp. 357, 360 (D. Mass. 1950).

of the Board, to whom outside counsel will report, may be preferable, and reporting lines should be established that are closely related to the way in which the client has been defined. Accordingly, care should be taken to insulate other board members and senior management from the conduct of the investigation so as not to prejudice the development of the investigation.

GATHERING EVIDENCE AND CONDUCTING INTERVIEWS OF WITNESSES

One of the first priorities of investigating counsel is to quickly gather all relevant documents and identify potential witnesses. These tasks will require that counsel promptly understand the nature of the company's business, its reporting processes and its policies and procedures. Time should be spent identifying the various categories of documents that could yield relevant information and knowledge.[47] This is an area where the retention of outside experts, such as forensic accountants or engineers, by counsel will be particularly useful.

Obtaining, Managing, and Analyzing Documents

In conducting any investigation, the two most important sources of information will be witness interviews and the documentary record. The two are interlocking, and effective management of each is essential to the proper execution of the other. Careful and thorough review of the documentary evidence is crucial for uncovering the underlying facts of an investigation. Especially where the conduct under investigation did not occur recently, documents are crucial to piecing together a coherent narrative, given that witness recollections may not be fresh. This section addresses the critical issues involved in ensuring the proper management and analysis of documents in the course of an internal investigation.

In structuring and conducting an investigation, counsel will be more effective if all relevant documents are identified, secured and analyzed. Counsel will need to be familiar with the types of documents that might be relevant to the investigation, the systems that the company uses to produce and store documents and the individuals within the company who are available to assist with document issues. Counsel will also have to implement an appropriate system for identifying and tracking documents. Finally, counsel may have to manage the simultaneous use of documents for the internal investigation, as well as for production in any parallel civil, criminal or regulatory proceedings.

From the outset, counsel should identify an individual or individuals within the company who can serve as a coordinator for document issues. This person will often be an in-house lawyer or paralegal who is not otherwise involved in the matters under investigation and who should have a good working knowledge of the company's document management systems and document retention policies. This person will need to be able to quickly identify for counsel potential sources of documents, as well as maintain a system for identifying which documents are new and which are duplicative of previously reviewed documents. This person will generally also be responsible for tracking document requests from litigation opponents, regulators or law enforcement, and ensuring that such requests are responded to in a timely and comprehensive fashion.

Document Preservation

Right from the outset of any investigation, counsel must takes steps to ensure that relevant documents are preserved, segregated and collected. If the investigation was initiated as a result of the company's receipt of a subpoena or document request, it is critical that all employees in possession of or with access to potentially relevant documents be instructed to refrain from altering, discarding, destroying or concealing any such documents. Even in the absence of a subpoena, a preservation notice is necessary to ensure that documents are not destroyed or disposed of in the ordinary course of business, so that they will be available to counsel in the course of conducting their investigation.[48] The credibility of the investigation will be seriously impaired by a failure to identify and secure relevant documents right from the start. For that reason, the scope and distribution of any document preservation notice should, at the outset of the investigation, err on the side of overinclusiveness. Employees should be encouraged to contact counsel or one of its agents with any questions regarding document preservation, and provided with instructions on how to do so.

At the start of the investigation, the company should immediately cease the regular deletion of relevant documents, including emails. Similarly, copies should be made or backup tapes pulled of relevant databases or similar resources. If appropriate, counsel or someone working under counsel's supervision should be sent to search for and retrieve documents from the various offices or off-site facilities where documents may be located.

[47] For instance, in a case involving potential accounting fraud, counsel should familiarize themselves with the relevant accounting reporting systems, and the internal processes followed by a company's financial management for assessing and externally reporting the company's financial results.

[48] The preservation notice should be directed not only at employees, but also at any third-party vendor who maintains documents or data for the company.

Employees should be provided a comprehensive list of the types of documents that they are to search for and provide to counsel. There should be explicit instructions to provide drafts and notes, in addition to finalized documents, as it will often be crucial to the investigative process to be able to track the evolution of particular documents over time. In addition, employees should be instructed to search for potentially relevant documents not only in their offices and workspaces, but also in any records in off-site storage, as well as their homes and personal offices and devices. Counsel may want to consider obtaining a written, signed certification from employees stating that they have provided all responsive documents and data. Such a certification will be useful to the company if additional documents from employees are identified in the course of a subsequent regulatory investigation. Efforts should also be made to obtain documents from former employees, even if they have no obligation to cooperate.

Careful attention should be paid to ensure the timely and comprehensive retrieval of electronic documents. In recent years, email has become perhaps the single most important source of information for the conduct of an investigation. Counsel must have access to personnel who understand the capabilities and limitations of the company's information systems, so that they will know exactly what is available, and how long it will take to retrieve that data.

Effective use of document management technology can greatly increase the efficiency and quality of an investigation. Counsel should seriously consider having all documents electronically scanned and catalogued as soon as they are gathered. The maintenance of such a database will provide the team with the ability to search and organize the vast amount of data that is collected in even smaller investigations, as well as to be able to retrieve and produce documents with a minimum of turnaround time. Counsel may choose to use the services of an outside vendor to handle this process.[49] Vendors will also be able to assist with copying and analyzing data sources such as hard drives, PDAs and encrypted files, should it become necessary in the course of the investigation. Vendors possess certain sophisticated search and management technologies that can drastically increase the efficiency of a document review by refining data sets to the most relevant information.

It is crucial for both the investigative process and for the credibility of the investigation that documents be carefully tracked throughout the investigation.

Organizing Document Review

It is crucial for both the investigative process and for the credibility of the investigation that documents be carefully tracked throughout the investigation. An individual or team should be designated to be responsible for managing documents as they are collected. A log or electronic identification system should be used to identify for each document its source, who possessed it, where it was found and the date that it was collected. It may be helpful to use an electronic numbering system for each of the documents, so that they can be tracked as they are used during the investigation. The document coordinator should retain all original versions of documents, so there are no chain-of-custody issues in any subsequent litigation.

When documents are received, they should be reviewed for relevance and privilege. Any documents that are determined to be privileged should be segregated immediately in order to prevent any inadvertent waiver of the privilege. Access to privileged documents should be limited to counsel and its agents. A privilege log should be maintained, in which the document number should be noted, as well as the date, the author, the recipients, and the basis on which privilege is being claimed. Regulators or civil litigants will frequently request such a log, and counsel will benefit greatly if it has tracked that information from the outset, rather than attempting to recreate it later in the investigation.

If possible, a preliminary list of potential interviewees should be assembled prior to the review of documents. This will allow reviewers to assemble sets of documents that are relevant to particular interviewees, so that they can be used to prepare for, or use in, the interviews. The reviewers should be cognizant of which names are or are not on the list, so that they can add new names as necessary, based on the contents of the documents being reviewed. It is often the case that the most informative witnesses are ones that were not known to the investigators at the outset of the investigation. In addition, documents should be identified and assembled by subject area. At the outset of the investigation, it is better to cast a wide net of potential interviewees and areas of interest. The topics of interest will likely change and be refined over the course of the investigation.

[49] If a vendor is used, the vendor should, for purposes of maintaining the privilege, be retained as an agent of counsel, rather than the company.

It is important that "hot documents" be identified and circulated to relevant personnel on the investigation team. The document coordinator should also maintain a file of these documents. In addition, the document coordinator should keep copies of all the different witness and topic binders, so that it is easy to determine what documents were shown to particular witnesses during their interviews. Counsel should take care to use numbered versions of the relevant documents in these binders, so that they may be easily cross-referenced with documents used in other contexts.

The document review team will also generally be responsible for assembling and maintaining a detailed chronology of the event or events under investigation. This chronology should be cross-referenced with the available documents, and should be continuously updated over the course of the investigation. For each event, the chronology should list, at a minimum, the date, the event and the source. If the source is a document, the chronology should note the author, any known recipients, and the custodian from whom the document was obtained.

Interviews

While considerable information may be gleaned from documents, interviews of individual employees, former employees and other personnel inside or outside of the firm are indispensable in fleshing out the meaning of documents, can help direct investigators to important documents, and generally help investigators evaluate facts and assess credibility. Because they assume such extensive importance in an investigation, particular care must be given to planning for and conducting witness interviews.

In many situations, it is beneficial to begin interviews at an early stage of an investigation, even before a significant number of documents have been reviewed. This will allow the investigators to get a greater understanding of the facts as quickly as possible and will "lock-in" the story of significant witnesses before they are influenced by other events. This strategy may only be advisable if the investigators will have more than one opportunity to interview a witness.

It may be advantageous to schedule interviews with lower level employees first, before speaking with more senior officials in the organization. In some situations, counsel will have only a single opportunity to interview senior officials, so it is best to do so only at a later stage in the investigation. Wherever possible, it is helpful to interview employees with information on similar subject matters in close proximity. It is also preferable to have the same counsel interview all employees who are able to provide similar types of information.

Counsel will not always be able to follow these strategies. For instance, government requests, employee resignations or disciplinary action may force counsel to interview some officials earlier than might otherwise be preferable. The persons to be interviewed, and the order of those interviews, should be frequently assessed. Counsel should be flexible to accommodate the exigencies and changes of the investigation. Counsel should also be prepared to conduct follow-up interviews, particularly where the initial interview took place at an early stage of the investigation, before counsel had an opportunity to review and digest many relevant documents.

Wherever possible, interviews should be staffed by two lawyers. Having two people present enables one individual to focus on conducting the interview while the other takes notes. Moreover, interviews should generally not be recorded or transcribed (to protect privileges and to avoid intimidating a witness), and having two people present can facilitate recollection of what a witness said on a particular subject. In addition, the recollections of two interviewers may be helpful if a witness subsequently denies a statement made during the interview

Given the significant exposure faced by individuals in internal investigations, it is increasingly common for employees to retain their own individual counsel. Retention of individual counsel should normally be allowed unless it unnecessarily delays or impedes the investigation. The company may be contractually or statutorily obligated to pay for counsel for an individual, and should evaluate whether it has such obligations at the outset of the investigation. Even if there is no legal obligation, the company may still decide to pay for counsel.[50]

If it is decided that counsel for individuals is necessary, steps should be taken to limit cost and inefficiencies. In some situations, individuals may need and want independent counsel. However, in other situations, it may be desirable for the company to recommend counsel for individuals whom the company believes will not be unduly disruptive to the investigation. It also may be possible, subject to conflicts, for that counsel to represent more than one employee in the investigation. Finally, it may further be appropriate for "shadow" counsel to be retained to consult with employees on an "as needed" basis.

At the beginning of every interview, counsel should provide what is commonly known as an "Upjohn warning."[51] This warning, at a minimum, specifies that counsel has been

[50] *See United States v. Stein*, 435 F. Supp. 2d 330, 340 (S.D.N.Y. 2006) for a discussion of relevant issues.

[51] These warnings evolved as a result of the Supreme Court's ruling in *United States v. Upjohn*, 449 U.S. 383 (1991).

retained to conduct an investigation, that the information obtained during the interview is privileged, that counsel does not represent the witness and that the decision whether or not to waive the privilege belongs solely to the entity that retained counsel to conduct the investigation.[52]

Such warnings are particularly important if the interviewee is a current employee and is not represented by individual counsel. Depending on the circumstances, additional warnings may be given. For example, it may be appropriate to disclose to witnesses that there is a related governmental investigation ongoing, that the company is cooperating fully with that investigation, that it may turn over notes of the interview to the government, or that the company intends to waive the privilege. Failure to make such disclosures could cause the witness to challenge the propriety of the interview and perhaps the investigation.[53]

Documents are indispensable in conducting interviews. Even where investigations are conducted in close temporal proximity to alleged misconduct, documents are often necessary to refresh a witness' memory. Strategic use of documents may also be helpful in assessing individual witnesses' credibility. Generally, it is useful to begin by asking relatively open-ended questions of witnesses without direct use of documents, in order to determine what the witness is able to remember independently.

Interviewers should generally avoid using questionnaires to elicit information from witnesses. In-person interviews (and to a lesser extent telephone interviews) will enable fuller communication, likely yield more information and provide a basis on which to assess the witness' credibility. Questionnaires also introduce significant privilege concerns, even though *Upjohn* makes it clear that responses to questionnaires are generally protected by the attorney-client privilege.[54] Because employee responses to questionnaires provide information unmediated by counsel, the work product protection that attaches to these materials may be more easily overcome. Thus, should a privilege be deemed to have been waived or never to have attached in the first place, information from employees presented to counsel may be deemed to be purely factual work-product, and more easily subject to discovery.[55] Questionnaires should therefore be used only sparingly and in connection with information that investigators determine would not pose a risk for the client. For instance, a questionnaire may serve a useful purpose of helping to narrow the scope of individuals to interview in person by inquiring as to the recipient's basic factual involvement with a particular transaction or set of events.

While many of the documents key to an investigation may be collected centrally through a corporation's information technology and records management personnel, it is critical that counsel ask interviewees whether they have additional documents in their possession not previously made available to counsel. Employees may have files in their office, at their homes or on cellphones, laptops or other personal computer devices. Witnesses should also be asked if they are aware of any relevant documents that have been destroyed.

Interviews should be memorialized in writing to maximize their utility to the investigation, particularly by promptly sharing key information from the interview with other team members, and to assist counsel in identifying any discrepancies in witness statements. Interviews should not be transcribed or recorded, however, because transcripts or recordings could be discoverable.[56] Memoranda of the interviews will be more likely to be protected by attorney-client and work product privileges to the extent they incorporate counsel's legal conclusions and mental impressions of the interview, rather than a verbatim transcript.[57] The need for accuracy in interview memos is obviously important and counsel should take the necessary time in an interview to make sure the witness' statements are understood.

To help preserve the attorney client privilege and work product doctrine, interview memos should be prominently marked "Attorney-Client Privilege" and "Attorney Work Product." In addition, an introduction to the summary should indicate that the interview was undertaken to render legal advice. The summary should also specify that the appropriate warnings were given to the employee and that the summary contains the mental impressions of counsel and does not represent a substantially verbatim transcript of the interview.

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[52] *See In re Grand Jury Subpoena: Under Seal*, 415 F.3d 333, 339-40 (4th Cir. 2005), cert. denied, 546 U.S. 1131 (2006) (holding that, after receiving Upjohn warning, employees "could not have reasonably believed that the investigating attorneys represented them personally," and therefore rejecting employees' attempt to prevent company's production of privileged interview memoranda on basis of assertion of joint defense privilege); cf. *United States v. LeCroy*, 348 F. Supp. 2d 375, 383 (E.D. Pa. 2005) (though implicit joint defense agreement may have existed, employees "voluntarily and knowingly waived" the protection of that agreement when they conducted interviews with company counsel after being advised that company might waive the privilege if government so requested).

[53] *See generally, U.S. v. Stein*, 440 F. Supp. 2d 315 (S.D.N.Y. 2006).

[54] Upjohn, 449 U.S. at 394-95.

[55] *See, e.g., In re John Doe Corp.*, 675 F.2d 482, 492 (2d Cir. 1982).

[56] *See, e.g., In re Royal Ahold*, N.V. Sec. & ERISA Litig. 230 F.R.D. 433, 436-37 (D. Md. 2005) (allowing discovery of typed memoranda of potential witnesses when contents of memoranda were "fairly straightforward recitation[s] of the information provided by the witness[es]"). Note that under Rule 26(b)(3) of the Federal Rules of Civil Procedure, a party to litigation has an absolute right to obtain "a statement concerning the action or its subject matter previously made by that party." FED. R. CIV. P. 26(b)(3), For purposes of the Rule, a "statement" is defined as "(A) a written statement signed or otherwise adopted or approved by the person making it, or (B) a stenographic, mechanical, electrical, or other recording, or a transcription thereof, which is a substantially verbatim recital of an oral statement by the person making it and contemporaneously recorded." Id. Interview memoranda that are not expressly adopted by the interviewee are not discoverable under Rule 26(b)(3). *See, e.g., Robinson v. Time Warner, Inc.*, 187 F.R.D. 144, 147 (S.D.N.Y. 1999).

[57] *See Upjohn*, 449 U.S. at 399 ("Forcing an attorney to disclose notes and memoranda of witnesses' oral statements is particularly disfavored because it tends to reveal the attorney's mental processes.").

THE INVESTIGATION'S AFTERMATH

REPORTING THE FINDINGS OF THE INVESTIGATION

The client likely will want some kind of report at the conclusion of the investigation, in either oral or written form, or both. This final report will be the culmination of the investigation, and may be the first time that the client is apprised of the key facts that were uncovered. It may also be the only opportunity for counsel to articulate the legal conclusions dictated by the findings of the investigation. For these reasons, one of the most important decisions the client will have to make is what form that report will take. The determination whether to produce an oral or a written report is not an easy one, as there are potentially important advantages and disadvantages to either approach. Counsel should understand the risks and benefits of both approaches, and should ensure that the client makes a careful and informed decision.

In the event that the client chooses to proceed with a written report, counsel must act carefully to ensure that it is drafted in such a manner so as to protect the client to the maximum extent possible, including the maintenance of all applicable privileges. This section explores the advantages and disadvantages of producing a written report of an internal investigation, what that report should look like and what alternatives exist. This section also addresses the issue of whether or not to provide the report to law enforcement or other regulators, or to release it publicly.

Advantages and Disadvantages of a Written Report

A written report can provide the client with all of the key facts and legal conclusions in a single document, allowing for informed consideration of any remedial or disciplinary actions to be taken. A written report also provides tangible evidence that the client (whether the company or the board) has sanctioned a thorough and complete examination of the issues being investigated. Written reports of internal investigations are frequently provided to regulators or law enforcement authorities in order to demonstrate cooperation. Finally, companies frequently use written reports of investigations to refute charges of wrongdoing in litigation.

In some cases, there is no practical choice other than producing a detailed written report. Both the SEC and DOJ have made numerous statements that credit may be given to companies that conduct internal investigations. Thus, companies may feel compelled to turn over the results of an internal investigation.

However, there are compelling arguments against producing a written report, and the decision to do so should not be entered into lightly. A written report will frequently contain findings or information that are potentially embarrassing or even damaging to the company. Even if the company intends to keep the report's findings confidential, maintaining the confidentiality of the written report can be exceedingly difficult. In addition, while the report may have some usefulness in dealing with regulators or law enforcement, it may also provide a roadmap for them to conduct their own investigations. It may also provide a similar roadmap to civil litigants, who otherwise might not become aware of the issues under investigation. Finally, statements in the written report may be used as "admissions" by the company under the Federal Rules of Evidence.[58]

Assuming that a thorough written report is not required to be produced, counsel should carefully review with the client the various alternatives. Two of the more common alternatives are either a limited written report or an oral report. A limited written report can include only certain of the issues investigated or be more of an executive summary without significant or identifying details (though, of course, it must still be accurate in what it does contain). An oral report provides the client with the necessary findings of the investigation without producing a written document that may be open to misinterpretation or misuse.[59]

Given the increased flexibility and protections of confidentiality attendant to the choice of an oral report over a written report, the oral report is an appealing alternative to a written report. However, there are drawbacks to this approach as well. If the existence of the investigation is already known to the public or regulators, the client's choice not to receive a written report of the investigation may expose the company to accusations that it is trying to conceal the

[58] *See* FED. R. EVID. 801(d)(2).

[59] Counsel's notes prepared for use in making an oral report are almost certainly protected from discovery by adverse parties as opinion work product.

findings of the investigation, or prevent particular facts from getting out. Indeed, if the findings of the report do not create a particularly high level of exposure for the company, it is quite possible that the perception created by the failure to obtain a written report could be more damaging to the company than would the release of those findings. The client will need to assess the relative benefits and dangers of each approach, and make a decision that maximizes the utility of the report, in whatever form, while minimizing the dangers, both legal and reputational.

Structuring the Report

The entire investigation should be conducted with an eye toward preparing some kind of final report and the decision whether to produce a written or an oral report can be made late in the process. It is imperative that counsel proceed with the utmost care in preparing the report. By recognizing the likely uses of the report, either by the client or by law enforcement, regulators or private litigants, counsel can prepare the report in a manner that best serves the client's interests. While the following section describes the preparation of a written report, the principles articulated apply equally to an oral report.

Even if it is decided early in the process to prepare only an oral report, counsel should begin assembling an outline of a report early in the investigative process. This outline should be protected by the work product doctrine. Facts can be added or changed to the outline as the investigation continues. In addition, the outline should contain cites of the source of the information so that it can be tracked quickly if necessary. What follows is a description of the various general subject matters that may be addressed by the report, along with a brief explanation of each.

Background and Mandate

The first section of the report should address the procedural background that led to the retention of counsel to conduct the investigation (*e.g.*, whether the investigation was precipitated by the receipt of a subpoena, a whistleblower letter, facts uncovered in testimony, etc.). This section should describe counsel's understanding of all of the events leading up to its retention. This section will lay out counsel's understanding of the posture of the matter prior to the investigation, in order to provide context to later portions of the report. If the investigation was undertaken pursuant to an outside mandate, such as from a bankruptcy examiner or as part of a settlement, that information should be disclosed in this section.

Perhaps most importantly, this first section should also contain an explicit identification of the client (*i.e.*, whether it is the company, the board, or a special committee) and a description of counsel's mandate in undertaking the investigation. The report should state in clear and precise terms exactly what issues counsel was hired to investigate, and what limitations, if any, were placed on counsel by the client. The report should state whether counsel was limited to investigating the matter that led to the investigation in the first place, or whether counsel had the discretion to explore any related matters as deemed appropriate. Finally, in order to obtain the maximum protection of the attorney-client privilege, when applicable, this section of the report should state explicitly that counsel was retained to provide legal advice to the client.

Executive Summary

This section should provide a summary of the findings and conclusions. This section makes it easier for the reader to review the report, particularly if the written report is extensive. Also, since the written report may be read by persons with different agendas and objectives, an executive summary should be written for readers with various perspectives.

Review of the Investigation

The next section should focus on reviewing the steps that counsel took in order to conduct the investigation. This section can note the time it took to conduct the investigation, the number of counsel who worked on the investigation, the total number of hours worked on the matter, the number and types of documents collected and analyzed, all of the locations visited and searched for relevant documents (including storage facilities), the number and identity of the people interviewed, and whether any outside experts were retained and consulted. It is also important to identify any witnesses who declined to cooperate or were otherwise unavailable to counsel, and the reasons they provided, as well as, to the extent possible, a description of any known documents or data that could not be reviewed. Finally, counsel should provide a narrative assessment of whether they believe they had sufficient cooperation from the client and others to conduct the investigation. Clients and others who are aware that this will be discussed in the report of an investigation may be more likely to be fully cooperative in the course of the investigation.

Findings

This section should lay out a narrative description of the relevant facts. The organization of this section will depend on the number and types of matters that were investigated. In some instances, this section may lay out the facts in chronological order, while in other instances it may make sense to group the facts by, for example, transactions, business groups or issues. However it is organized, this section may include either a detailed recitation of the facts or a more summary-type description.

The contents of this section will serve as the basis for the later legal conclusions and recommendations. To the extent that the report will include significant details, it is crucial to the credibility of the report as a whole that counsel should be able to identify the basis for each and every statement in this section. If assertions by witnesses are contradictory, or conflict with documentary evidence, that should be stated clearly, but in a non-inflammatory manner, focusing only on the fact of the inconsistency.[60] Any areas where counsel was unable to verify information or where there are questions as to the accuracy or authenticity of particular documents or information should also be noted and explained.

Conclusions

This section is significant as it provides an assessment of the potential legal vulnerabilities of the company based on the facts identified during the investigation. The report should lay out the legal standards used, and should be limited to only those facts that were discussed in the "Findings" section.

The structure of this section is heavily dependant on the purpose of the investigation. If, for example, the investigation was intended to determine the pervasiveness of a particular practice within a company, the legal conclusions section may focus on the potential liability of the company and particular employees for offenses related to that practice. On the other hand, if the investigation is being undertaken as, for example, counsel to a bankruptcy examiner, the focus of the legal conclusions may be an assessment of the relative strength of the bankruptcy estate's claims for recoveries against various parties.

In laying out its legal conclusions, counsel may want to address not just those laws that may have been violated, or those claims that can be asserted, but also violations or claims that it considered but found lacking in support. This can help the client by providing a framework for analyzing potential culpability should new information come to light. More importantly, a well-reasoned discussion of why the company's conduct was not violative of any law or regulation can be used by the company to persuade the relevant authorities that charges against the company are not warranted.

Recommendations

To the extent requested by a client, there may be a section on counsel's recommendations for any actions it believes the company should or is compelled to take. The types of recommendations which are generally included in such reports include:

- Personnel actions, such as firing, suspending, reassigning, or otherwise disciplining particular employees;
- Structural reforms, such as changes to reporting lines or review structures, the creation of new committees or positions, the elimination of particular business practices, or even the sale of part or all of the company;
- Improvements to the company's internal control processes;
- Description of areas requiring additional scrutiny, whether by the same counsel or as part of a separate investigation;
- Legal actions to be taken by the company, such as a civil suit, regulatory action, or filing for bankruptcy protection.

Careful attention should be given if recommendations are made. If the company declines to follow the recommended course of action, it may expose itself to scrutiny by regulators or civil litigants.[61] Therefore, counsel should be wary of the potentially burdensome effects of its recommendations (both individually and cumulatively) as it crafts this section of the report.

The elements of an effective report of the investigation will be the same no matter what form the report takes. Even if no written report is produced, counsel should be prepared to address all of the topics noted above in an oral report. By keeping these elements of the final report in mind during the course of the investigation, counsel will be able to conduct the investigation in a manner calculated to maximize its utility to the client.

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[60] As a general matter, statements presented as "facts" are more vulnerable to later claims of defamation than those clearly characterized as "opinion." *See, e.g., Pearce v. E.F. Hutton Group, Inc.*, 664 F. Supp. 1490, 1500 (D.D.C. 1987) (noting, in the context of discussing a defamation suit by a company employee against the author of an investigative report, that "statements of opinion are absolutely exempt from libel suits under the first amendment.") (citing *Gertz v. Robert Welch, Inc.*, 418 U.S. 323 (1974)). Therefore, to avoid potential defamation claims from employees who are included in the report, it is important to clearly note that any judgment as to the employee's veracity is counsel's opinion, in light of the known facts. This may provide some measure of protection under the absolute exemption for opinions referenced in *Pearce*.

[61] *See, e.g., SEC v. Stratton Oakmont, Inc.* 878 F. Supp. 250, 254 (D.D.C. 1995) (SEC obtained a permanent injunction against brokerage firm for failing to implement recommendations of court-ordered monitor).

Disclosure of the Report

After the completion of the investigation, the company will be faced with the question of whether or not to disclose the report or the findings of the investigation, and if so, how it will go about doing so. With respect to the first issue, whether the report or the findings should be disclosed at all, the answer will depend first on whether the company is legally obligated to make such disclosure. Even if no legal obligation exists, the company may nevertheless choose to voluntarily disclose the findings. Whether by compulsion or by choice, the disclosures must be handled with recognition of the likely consequences of making public such sensitive information about the workings and conduct of the company, as well as with an eye towards maintaining any available protections for information that is not part of the company's disclosures.

Required Disclosure

At the conclusion of the investigation, counsel and the client should carefully analyze the nature of the information uncovered in the course of the investigation, as well as the legal conclusions laid out by counsel, to determine whether any agreements, statutes, regulations or other legal rules require some disclosure by the company. In some instances, the company may be committed to make some disclosure as a condition of a previous agreement or settlement. Regulators will sometimes require as part of a settlement a company to appoint an independent person to conduct an internal investigation to examine the pervasiveness of a particular practice within that company and prepare a written report to be turned over to the regulator.[62]

Publicly reporting companies must make a separate determination of whether they are required to disclose in a public filing the findings of an internal investigation. In some instances, disclosure may be required by specific regulations that require public companies to disclose certain facts or events to investors. For instance, evidence of certain environmental compliance issues may require specific disclosure.[63] Similarly, companies that do business with the federal government are required to disclose in writing to the Inspector General of the contracting agency if the company has "reasonable grounds" to believe that kickbacks may have been paid.[64] Federally insured banks are subject to similar requirements if they believe they have been defrauded.[65]

As to other types of misconduct, while the company is not required to disclose any and all negative facts in its possession, the rules governing the content of filings under both the Securities Act and the Securities Exchange Act mandate that those filings must include material information if that information is needed to make any of the company's statements not misleading.[66] Materiality, in this context, is defined as information of which there is a "substantial likelihood that a reasonable shareholder would consider it important."[67] If the investigation did uncover evidence of illegal activity by the company or its agents, the weight of authority holds that there is no requirement that the company disclose its illegal conduct unless such disclosure is necessary to make other statements not misleading.[68] The SEC also may take the position that ethical lapses by senior officers of a company are material. While these rules dictate that certain information may be required to be disclosed in some instances, it will rarely be the case that the entire report of the investigation must be disclosed. However, the company should be aware of the danger of selective disclosure, as the sharing of the report with some investors but not others would almost certainly constitute a violation of Regulation FD.[69]

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[62] *See, e.g., SEC v. Time Warner Inc.*, Litig. Release No. 19147, 2005 SEC LEXIS 649, at *2 (Mar. 21, 2005) (announcing agreement of Time Warner to settlement terms that included retention of independent examiner to determine accuracy of company's past accounting).

[63] *See* 17 C.F.R. § 229.101(c)(xii) (Regulation S-K) (2006) ("[a]ppropriate disclosure . . . shall be made as to the material effects that compliance with [environmental regulations] may have upon the capital expenditures, earnings and competitive position of the registrant").

[64] See Anti-Kickback Enforcement Act of 1986, 41 U.S.C. § 57 (2006). Several states have similar statutes for companies doing business with that state.

[65] *See* 12 C.F.R. § 21.11 (2006), which requires federally insured banks to submit "Suspicious Activity Reports" in writing to the Office of Comptroller of the Currency.

[66] *See*, e.g., Exchange Act §10(b); Exchange Act §12b-20; 17 C.F.R. § 229.303(a)(3)(ii) (2006) (Regulation S-K) (requiring MD&A disclosure to include "any known trends or uncertainties that have had or that the registrant reasonably expects will have a material . . . unfavorable impact" on the company's net sales or revenues).

[67] *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976). There must also be "a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." *Basic Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988).

[68] Courts have consistently held that, absent an affirmative duty to disclose under a particular law or regulation, there can be no criminal liability for failure to disclose uncharged wrongful conduct. *See United States v. Matthews*, 787 F.2d 38, 49 (2d Cir. 1986) (holding that uncharged criminal conduct need not be disclosed in proxy statements pursuant to Rule 14a-9); *United States v. Crop Growers Corp.*, 954 F. Supp. 335, 346-47 (D.D.C. 1997); In the civil context, courts have reached conflicting decisions. *Compare Roeder v. Alpha Indust., Inc.*, 814 F.2d 22, 28 (1st Cir. 1987) (holding that plaintiff had failed to state a claim for a violation of Rule 10b-5 against defendant for failing to disclose, until indictment was imminent, bribery payments by executive, because, even if payments were material, no duty to disclose existed); *Menkes v. Stolt-Nielsen S.A.*, No. 3:03cv409, 2005 U.S. Dist. LEXIS 28208, at *28-29 (D. Conn. Nov. 10, 2005) ("Rule 10b-5 generally does not 'require management to accuse itself of antisocial or illegal policies'" (quoting *Amalgamated Clothing & Textile Workers Union, AFL-CIO v. J.P. Stevens & Co.*, 475 F. Supp. 328, 331 (S.D.N.Y. 1979), *vacated as moot*, 638 F.2d 7 (2d Cir. 1980)); *Galati v. Commerce Bancorp, Inc.*, No. 04-3252, 2005 U.S. Dist. LEXIS 26851, at *17 (D.N.J. Nov. 7, 2005), aff'd, No. 05-5157, 2007 U.S. App. LEXIS 7315 (2007) (citing *Roeder*); *with SEC v. Fehn*, 97 F.3d 1276, 1290-91 (9th Cir. 1996), cert. denied, 522 U.S. 813 (1997); *In re Par Pharm., Inc. Sec. Litig.*, 733 F. Supp. 668, 675 (S.D.N.Y. 1990) (plaintiffs stated 10b-5 claim when they alleged that defendant corporation had failed to disclose allegedly illegal payments to government officials to speed drug approval process, but had touted company's ability to obtain such approvals without describing how); *Ballan v. Wilfred Am. Educ. Corp.*, 720 F. Supp. 241, 249 (E.D.N.Y. 1989) (defendant violated Rule 10b-5 when it failed to adequately and timely disclose that it was likely to be indicted for failure to comply with government regulations regarding student loan applications); *Cf. In re Teledyne Def. Contracting Derivative Litig.*, 849 F. Supp. 1369, 1382-83 (C.D. Cal. 1993) (neither investigation nor underlying fraudulent conduct are required to be disclosed until charged or proven).

[69] 17 C.F.R. § 243 (2006).

Voluntary Disclosure

Even when the company is not compelled to make disclosure of the findings of the investigation, there are still reasons to consider voluntarily disclosing those findings. Voluntary disclosure allows the company to control the timing, content and manner of any release of news to the public, and can be of significant use to the company in attempting to manage the potential adverse consequences of disclosure. In addition, there may be certain legal and/or regulatory advantages to making a full and voluntary disclosure. However, in practical terms, some of these advantages may be overstated.

In circumstances where information about the investigation or the underlying conduct has already become public, the company can use the public disclosure of the investigation findings as a method of trying to regain some measure of control over public perception. A thorough, well-written report can be used to refute any inaccurate information that may have been disseminated. Even if the report has uncovered wrongdoing, the company may feel a frank and forthcoming appraisal of its own behavior will resonate positively with investors and the public generally. This tactic may be especially attractive to the company in instances where the wrongdoing was of a less serious nature (*i.e.* where there is likely no criminal or material financial exposure for the company), or was restricted to the actions of a limited number of individuals. In such circumstances, the public release of the report is more likely to provide at least a measure of finality to the investigation. Even if the potential consequences of the underlying conduct are more severe, the company may choose to make full public disclosure in order to begin to restore public confidence by getting all of the "bad news" out at one time, as opposed to piecemeal revelations that might constantly raise suspicion regarding what further news might emerge. If it is decided to release publicly a report, it may be useful for public companies to provide a copy to the SEC beforehand.

If a report is not publicly disclosed, the company may decide to disclose the results of the investigation to regulatory or law enforcement officials. The company may seek to forestall potential regulatory action or criminal prosecution by presenting the underlying facts in a manner more favorable to the company. Such a disclosure can be a means for the company to present to authorities any argument or authority that may dissuade them for taking action against the company, or to be more lenient in settlement discussions.

In recent years, the SEC and other government authorities have increasingly sought to encourage voluntary disclosure of misconduct by companies. A notable example of this has been in the Justice Department's guidelines for prosecution of corporate entities, the "McNulty Memorandum," named after its author, Deputy Attorney General Paul McNulty.[70] The McNulty Memorandum dictates that one of the considerations for prosecutors to take into account in assessing whether a corporation's cooperation with government investigators is sufficient to prevent an indictment is "the corporation's timely and voluntary disclosure of wrongdoing . . . ."[71]

The McNulty Memorandum was followed in 2008 by a Memorandum by Deputy Attorney General Mark Filip. The Filip Memorandum confirmed that the DOJ "understands that the attorney-client privilege and attorney work product protection are essential and long-recognized components of the American legal system."[72] The Filip Memorandum further stated that cooperation credit would be based on the disclosure of the "relevant facts" and not on the waiver of the attorney-client privilege or the attorney work product protection.

Recently, the DOJ has indicated that it will place increased emphasis on the prosecution of individuals in corporate crime cases and will rely on the Filip Factors to encourage corporate cooperation in these efforts, including "in the investigation of its agents."[73] In his September 2014 remarks, Principal Deputy Assistant Attorney General for the Criminal Division Marshall L. Miller stated that "[v]oluntary disclosure of corporate misconduct does not constitute true cooperation, if the company avoids identifying the individuals who are criminally responsible."[74] According to Mr. Miller, the DOJ will deny cooperation credit to companies who fail to provide information and evidence about executive and employee criminal misconduct.[75] These points were reiterated by Deputy Assistant Attorney General Sung-Hee Suh in January 2015.[76]

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[70] The McNulty Memorandum was an update of an earlier version of the guidelines (known as the "Thompson Memorandum," after its author, former Deputy Attorney General Larry Thompson). The McNulty Memo was issued in response to wide-ranging criticism of the Justice Department's perceived insistence on companies waiving the attorney-client privilege in order to obtain credit for cooperating with prosecutors. As stated in the McNulty Memorandum, companies can receive credit for waiving the privilege, but may not be penalized for not doing so. McNulty Memorandum at § VII.B.2. *See* U.S. SENTENCING GUIDELINES MANUAL § 8C2.5(g) (2006) (allowing for lowering of sentence if defendant organization has "within a reasonably prompt time after becoming aware of the offense, reported the offense to appropriate governmental authorities, fully cooperated in the investigation, and clearly demonstrated recognition and affirmative acceptance of responsibility for its criminal conduct").

[71] McNulty Memorandum at § III.A.4.

[72] Filip Memorandum (August 28, 2008) at 8.

[73] *Id.* at 4.

[74] Marshall L. Miller, U.S. Dep't of Justice Principal Deputy Assistant Attorney General for the Criminal Division, Remarks at the Global Investigation Review Program (Sept. 17, 2014) (discussing Filip Factor Four) (transcript available at www.justice.gov/criminal/pr/speeches/2014/crm-speech-1409171.html).

[75] Mr. Miller specifically identified two cases in which corporations "paid a historic price not only for their criminal conduct, but also for their insulation of culpable corporate employees." *See, e.g., United States v. BNP Paribas SA*, No. 1:14-cr-00460-LGS (S.D.N.Y. 2014) and *United States v. Credit Suisse AG*, No.1:14-CR-188, 2014 WL 5026739 (E.D. Va. 2014)).

[76] Sung-Hee Suh, U.S. Dep't of Justice Deputy Assistant Attorney General for the Criminal Division, PLI's 14th Annual Institute on Securities Regulation in Europe: Implications for U.S. Law on EU Practice (Jan. 20, 2015) (transcript available at www.justice.gov/opa/pr/deputy-assistant-attorney-general-sung-hee-suh-speaks-pli-s-14th-annual-institute-securities).

Similarly, the SEC has also taken steps to encourage corporate and individual cooperation with investigations. In the 2001 Seaboard Report laying out its criteria for assessing cooperation by companies who have engaged in potentially violative conduct, the SEC suggested that it seeks an affirmative response to all of the following questions:

> Did the company promptly make available to our staff the results of its review and provide sufficient documentation reflecting its response to the situation? Did the company identify possible violative conduct and evidence with sufficient precision to facilitate prompt enforcement actions against those who violated the law? Did the company produce a thorough and probing written report detailing the findings of its review? Did the company voluntarily disclose information our staff did not directly request and otherwise might not have uncovered? Did the company ask its employees to cooperate with our staff and make all reasonable efforts to secure such cooperation?[77]

Additionally, in 2010 the SEC announced the creation of its Enforcement Cooperation Program.[78] Borrowing from the approach used by DOJ and other agencies, the SEC announced that it would assess the actions of entities and individuals to determine when it may be appropriate to give credit for cooperation. Since this program took effect, the SEC has repeatedly provided such credit through the use of cooperation agreements, deferred prosecution agreements, and non-prosecution agreements.[79]

The benefits of seeking credit for cooperation are clear. In many cases, it is both necessary and appropriate for the company to take any steps reasonably available to it in order to avoid indictment or a fraud accusation. However, both the Justice Department and the SEC are extremely exacting in their assessment of cooperation, and will frequently make additional demands on the company beyond the disclosure of an independent investigation.[80] By making such an approach to the authorities, the company may find itself without any further leverage against the ever-increasing demands of the government investigators. For this reason, the company may find that it has sacrificed more than it has gained when it takes the dramatic step of voluntarily producing its findings.

Disclosure of the report, whether to the public or to the government, may also create significant pressure on the company to take disciplinary action against the individuals identified as having participated in any wrongdoing. By exposing these identities to the public, the company may lose the flexibility to make its own determination of the appropriate punishment for the various levels of culpability typically found in an internal investigation.[81] Similarly, the company may find itself subject to public pressure to constrain or abandon certain business or governance practices that were the subject of the investigation. By publicizing the results of the investigation, a situation is created where failure to take certain remedial action may cause the company to be perceived as indifferent to or ignoring perceived responsibilities. This pressure may undermine the company's ability to act without public influence.

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[77] Seaboard Report, Exchange Act Release No. 44069, 2001 SEC LEXIS 2210, at *8. The Environmental Protection Agency has adopted similar standards. See Environmental Protection Agency, INCENTIVES FOR SELF-POLICING: DISCOVERY, DISCLOSURE, CORRECTION AND PREVENTION OF VIOLATIONS, (2000) (civil); EARL E. DEVANEY, ENVIRONMENTAL PROTECTION AGENCY OFFICE OF CRIMINAL ENFORCEMENT: THE EXERCISE OF INVESTIGATIVE DISCRETION (1994) (criminal).

[78] SEC Release No. 2010-6, SEC Announces Initiative to Encourage Individuals and Companies to Cooperate and Assist in Investigations (Jan. 13, 2010) (available at http://www.sec.gov/news/press/2010/2010-6.htm). In March 2014, the SEC launched a similar initiative targeted to municipal issuers and underwriters. SEC Release No. 2014-46, SEC Launches Enforcement Cooperation Initiative for Municipal Issuers and Underwriters (March 10, 2014) (available at http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370541090828).

[79] *See, e.g.*, SEC Release No. 2010-252 (Dec. 20, 2010) (detailing SEC's first non-prosecution agreement, entered into with Carter's Inc. in connection with *SEC v. Elles*, Civ. Action No. 1:10-CV-4118 (N.D. Ga. 2010)), available at http://www.sec.gov/news/press/2010/2010-252.htm; SEC Release No. 2011-112 (May 17, 2011) (describing SEC's first deferred prosecution agreement, entered into with Tenaris S.A.), available at http://www.sec.gov/news/press/2011/2011-112.htm; and SEC Release No. 2013-241 (Nov. 12, 2013) (detailing SEC's first deferred prosecution agreement with an individual (Scott Herckis) in connection with *SEC v. Berton M. Hochfeld et al.*, Civ. Action No. 12-CV-8202 (S.D.N.Y.2012)), available at http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370540345373.

[80] Disclosure to governmental authorities has certain other risks. In two instances, the government has brought obstruction of justice charges against executives who provided or caused to be provided false or misleading information to counsel conducting an internal investigation of their employer. In both cases, the charges were brought under 18 U.S.C. § 1512(c)(2), which makes liable anyone who "corruptly . . . obstruct[s], influence[s], or imped[es] any official proceeding." The charge was first used in this context in 2004, when federal prosecutors charged several former executives of Computer Associates, Inc., with obstruction in connection with allegedly false statements that the executives made to outside counsel in the course of an internal investigation of accounting fraud at the company. The government's case rested on the theory that the executives were aware of the company's intention to provide the results of the investigation to the government. *See, e.g., Information, United States v. Woghin*, Cr. No. 04-847 (E.D.N.Y) (Sept. 22, 2004); Information, *United States v. Kaplan*, Cr. No. 04-330 (E.D.N.Y.) (Apr. 8, 2004). The SEC, in the civil context, included similar charges against the executives. *See, e.g., SEC v. Computer Assocs. Int'l Inc.*, Litig. Release No. 18891, 2004 SEC LEXIS 2157, at *6 (Sept. 22, 2004). The Deferred Prosecution Agreement with Computer Associates itself makes reference to the obstruction by its executives as well. *See supra* note 20. Then, in 2006, the United States District Court for the Southern District of Texas refused to dismiss the indictment of a gas trader who was charged under § 1512(c) (2) with lying to counsel conducting an internal investigation relating to charges of false reporting of gas prices by the trader, marking the first time this theory had survived judicial scrutiny. *See United States v. Singleton*, 178 F. App'x 259 (S.D. Tex. 2006), *cert. denied*, 127 S. Ct. 420 (2006).

[81] The public disclosure of the report also exposes the company to potential libel claims by the individuals identified. See, e.g., Pearce v. E.F. Hutton Group, Inc., 664 F. Supp. 1490 (D.D.C. 1987), where former United States Attorney General Griffin Bell, then in private practice, was sued for stating in an investigative report (the findings of which were disclosed publicly at a press conference) that, inter alia, as to plaintiff's conduct, "no reasonable person could have believed that this conduct was proper," that the plaintiff had "actually engaged in wrongdoing," and that the plaintiff was "a moving force in improprieties." Id. at 1501. The court, noting the widespread dissemination of the report (via the press conference) rejected Bell's contention that the statements in the report should be protected by the "absolute privilege" that attaches to statements of opinion, and instead ruled that a negligence standard should apply. Id. at 1503-06. For a fuller discussion of the potential exposure of counsel to libel claims for investigative reports, see Edwin G. Shallert & Natalie R. Williams, Report of the Investigation, in INTERNAL CORPORATE INVESTIGATIONS (Brad D. Brian & Barry F. McNeil eds., 2d ed. 1993).

The biggest drawback to voluntary disclosure is the likelihood that such disclosure will lead to the loss of the attorney-client privilege, or even of work product protection, for not only the report, but for the underlying documents and investigative record as well. While exceptions exist, as a general rule, disclosure to the government of the report of an internal investigation will serve as a waiver of the privilege as to that report, and thus expose it to discovery by civil litigants. Thus, while the company may desire to avail itself of the opportunity to receive credit for cooperation with government investigators by turning over the report, it needs to recognize that the report may be discoverable in any parallel civil proceedings as well.

Companies have frequently attempted to argue that an independent report should remain protected from discovery on the basis of a finding that there was only a "selective" or "limited" waiver of the attorney-client privilege. The Eighth Circuit, in its 1977 decision in *Diversified Indus., Inc. v. Meredith*, held that the plaintiff company's disclosure to the SEC, pursuant to a subpoena, of certain privileged information developed in the course of an internal investigation did not constitute a blanket waiver of the attorney-client privilege.[82] The court reasoned that "[t]o hold otherwise may have the effect of thwarting the developing procedure of corporations to employ independent outside counsel to investigate and advise them in order to protect stockholders, potential stockholders and customers."[83] A limited number of other courts have also acknowledged the possibility of limited waiver, though typically relying on the existence of a confidentiality agreement between the disclosing party and the government as a basis for their finding.[84]

The vast majority of courts that have examined the issue, however, have rejected the selective waiver theory, though they have differed to some extent on the scope of the waiver effected after disclosure to the government.[85] Most of the objections to the theory of selective waiver center around the premise that the privilege only attaches to those communications that are not intended to be revealed to third parties and that selective waiver will allow the abrogation of that confidentiality only when it benefits the company.[86] In the face of the overwhelming reluctance of courts to accept selective waiver, there has been some pressure to create by legislative action a statutory exemption from total waiver in order to incentivize companies to share investigative reports with government prosecutors.

Though courts have been resistant to attempt to maintain the confidentiality of the report once it has been disclosed to the government, there are certain steps a company can take in order to maximize its control of where and how the report is used. Certain courts have held that disclosure made to the government pursuant to a subpoena may not act as a blanket waiver of all protections.[87] Therefore, the company may want to consider requesting that the government issue a formal request for the document prior to turning it over. In addition, the company should try to obtain a signed confidentiality agreement from the government prior to turning over the report. At a minimum, the agreement should state that the disclosure of the report is not intended as a waiver of any privilege, and that the government will not contend that such a waiver has taken place. The agreement should also bar the government from unilaterally disclosing the contents of the report to third parties, including, if possible,

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[82] *Diversified Indus, Inc. v. Meredith*, 572 F.2d 596, 611 (8th Cir. 1977).

[83] *Id.*

[84] *See, e.g., Dellwood Farms, Inc. v. Cargill, Inc.*, 128 F.3d 1122, 1126-27 (7th Cir. 1997); In re Steinhardt Partners, L.P., 9 F.3d 230, 236 (2d Cir. 1993). Other courts have explicitly rejected this rationale. See, e.g., In re Columbia/HCA Healthcare Corp. Billing Practices Litig., 293 F.3d 289, 302 (6th Cir. 2002), cert. dismissed, 539 U.S. 977 (2003). In addition, certain courts have suggested that waiver may be avoided if the company can show that the protected information was shared with the government in furtherance of "a common interest in developing legal theories and analyzing information." See Steinhardt, 9 F.3d at 236; *In re Cardinal Health, Inc. Sec. Litig.*, No. M8-85, 2007 U.S. Dist. LEXIS 36000, at *26-28 (S.D.N.Y. Jan. 26, 2007) (citing Steinhardt and holding that Audit Committee's investigation of potential financial misstatements, undertaken after commencement of SEC and DOJ investigations and with the intention to be shared with those agencies, was for purpose of ensuring that company's accounting and financial practices be clean, and that, as such, the Audit Committee's interests were "in common" with SEC and DOJ); In re LTV Sec. Litig., 89 F.R.D. 595, 614-15 (N.D. Tex. 1981) (after agreeing in consent decree to appointment of special investigatory officer, SEC and corporation shared common interest in analyzing facts and legal theories, and therefore no waiver took place upon sharing of documents with SEC).

[85] *See, e.g., In re Qwest Commc'n Int'l, Inc.*, 450 F.3d 1179, 1201 (10th Cir. 2006), *cert. denied*, 127 S. Ct. 584 (2006) (collecting cases, and rejecting selective waiver of both attorney-client privilege and work product protection); *Columbia/HCA*, 293 F.3d at 302 (same); *United States v. Mass. Inst. of Tech.*, 129 F.3d 681, 687-88 (1st Cir. 1997) (same); *Westinghouse Elec. Corp. v. Republic of Philippines*, 951 F.2d 1414 (3rd Cir. 1991) (same); *In re Royal Ahold N.V. Sec. & ERISA Litig.*, 230 F.R.D. 433 (D. Md. 2005) (same); *cf. In re Martin Marietta Corp.*, 856 F.2d 619, 625-26 (4th Cir. 1988), *cert. denied*, 490 U.S. 1011 (1989) (disclosure waived as to non-opinion work-product, but not as to opinion work product); *Permian Corp. v. United States*, 665 F.2d 1214, 1222 (D.C. Cir. 1981) (disclosure to government waived attorney-client privilege but not work-product protection); I*n re Worlds of Wonder Sec. Litig.*, 147 F.R.D. 208 (N.D. Cal. 1992) (same); *SEC v. Beacon Hill Asset Mgmt. LLC*, 231 F.R.D. 134, 142-43 (S.D.N.Y. 2004) (disclosure waives attorney-client privilege and work product protection to extent necessary to verify information in the report, but does not operate as a subject-matter waiver of work product protection). Recent state court decisions have similarly rejected assertions of selective waiver. *See, e.g., McKesson Corp. v. Green*, 610 S.E.2d 54, 56 (Ga. 2005); *McKesson HBOC, Inc. v. Superior Court*, 115 Cal. App. 4th 1229, 1236-42 (App. Ct. 2004).

[86] *See, e.g., Columbia/HCA*, 293 F.3d at 302 ("[A]ny form of selective waiver, even that which stems from a confidentiality agreement, transforms the attorney-client privilege into merely another brush on an attorney's palette, utilized and manipulated to gain tactical or strategic advantage.") (quotations omitted); Permian, 665 F.2d at 1221 ("The client cannot be permitted to pick and choose among his opponents, waiving the privilege for some and resurrecting the claim of confidentiality to obstruct others, or to invoke the privilege as to communications whose confidentiality he has already compromised for his own benefit . . . . The attorney-client privilege is not designed for such tactical employment.").

[87] The Second Circuit in particular has focused on the issue of the company's intent to maintain the confidentiality of the report in deciding whether a waiver has occurred. *Compare In re Leslie Fay Cos. Sec. Litig.*, 161 F.R.D. 274, 282-84 (S.D.N.Y. 1995) (holding no waiver when company had obtained "explicit confidentiality agreements with the authorities . . . ."), *with Bank of Am., N.A. v. Terra Nova Ins. Co.*, 212 F.R.D. 166, 172-73 (S.D.N.Y. 2002) (waiver found when work-product disclosed to law enforcement agency "without any agreement regarding confidentiality").

other government entities.[88] Some courts have held that such agreements are sufficient to prevent a limited waiver of at least the protection of the work-product privilege, if not of the attorney-client privilege, and could therefore help the company avoid the potential disclosure of not only the report but the underlying documentary record of the investigation as well.[89]

In addition, courts have focused on the manner in which the report is used in determining whether a waiver has taken place. Specifically, several courts have found that a waiver occurred when the company undertook the "offensive" use of the report, by, for example, basing its defense on the existence of an exculpatory investigative report, while simultaneously asserting that the report is privileged.[90] Therefore, the company may have a better chance of preserving privileges with respect to the report if it bases its defense on the underlying facts developed in the report, rather than the report itself.

DISCIPLINING EMPLOYEES

Many internal investigations will lead at some point to the company disciplining or even terminating an employee, whether a low-level "rogue" employee, or senior officer who failed to prevent a problem. Sometimes it is a result of the facts or conduct underlying the reasons for the investigation having been initiated in the first place. Other times, the employee's actions in the course of the investigation may lead the company to punish that person. The company also may take disciplinary action in order to satisfy the explicit or perceived demands of regulators, prosecutors or external auditors. In each of these situations, the company must take great care to act in a manner that will not either create new problems or exacerbate those problems that sparked the internal investigation to begin with.

When actual or potential employee wrongdoing comes to light, several competing considerations must be weighed in determining the appropriate course of action for the company. The effect on the company's other employees, ongoing operations, the continuing investigation and the company's relations with regulators and/or law enforcement are all part of the equation. In addition, there are varying degrees of discipline, ranging from a written reprimand to termination. How the company balances these considerations is necessarily a function of both the timing and the precipitating cause of the disciplinary action. Each will have an effect on the decisions of whether, when and how to discipline an employee.

Discipline for Failing to Cooperate with the Investigation

In certain instances, employees may refuse to cooperate with the company's internal investigation. In the vast majority of circumstances, there is no Fifth Amendment right against self-incrimination in the context of an internal investigation by a private employer.[91] However, the company should consider several factors in choosing whether to punish an employee in such a situation. First and foremost is the question of why the employee is refusing to cooperate. The employee's resistance may be indicative of the existence of additional, undiscovered issues for the company to explore as part of its investigation. Alternatively, the employee's lack of cooperation may be a signal that the perception by the employees of the investigation itself is that it is not being pursued in an evenhanded manner. Even if the company chooses to terminate the employee for not cooperating, it should still undertake to understand the reasoning behind the employee's decision.

Terminating an employee who refuses to cooperate should not be done reflexively. Taking action against an employee can have serious consequences for the company, from antagonizing other employees to instigating a civil suit by the fired employee. Prior to taking any such action, the company should take into account the seriousness of the investigation, the basis for the employee's refusal to cooperate, the company's treatment of similarly situated employees, and whether the information sought is available by alternative means.

It should be recognized that regulators or prosecutors may not look favorably on the company if it fails to discipline appropriately an employee who refuses to cooperate with an internal investigation. If the company is perceived to be encouraging, implicitly or explicitly, the intransigence of its employees, it may have a negative effect on the company's ability to receive credit for cooperating with investigating authorities. Therefore, the company should document its attempts to encourage employee cooperation with the internal investigation. For example, the company should make

[88] In at least one case, a court rejected a claim of selective waiver despite the presence of a confidentiality agreement with the SEC, because the agreement permitted the SEC to disclose information as required by law or in furtherance of its discharge of its duties and responsibilities. The court determined that such an agreement was "conditional," and therefore "inconsistent with those cases . . . allowing selective waiver." *See In re Syncor ERISA Litig.*, 229 F.R.D. 636, 646 (C.D. Cal. 2005).

[89] *See, e.g., In re Royal Ahold N.V. Sec. & ERISA Litig.*, 230 F.R.D. 433, 436-37 (D. Md. 2005).

[90] *See, e.g., Granite Partners, L.P. v. Bear, Stearns & Co.*, 184 F.R.D. 49, 55 (S.D.N.Y. 1999) ("Waiver typically occurs when the party asserting the privilege placed a protected document in issue through some affirmative act intended to insure [sic] to that party's benefit or where the party makes selective use of the privileged materials.") (citation omitted).

[91] *See Nuzo v. Northwest Airlines, Inc.*, 887 F. Supp. 28, 33 (D. Mass. 1995).

sure that the individual has been fully informed of both his obligation to cooperate and the potential consequences for not doing so.

In the event that the company chooses to discipline an employee for failing to cooperate with an internal investigation, counsel should be consulted prior to any action being taken. State law in the relevant jurisdiction may require that the company only terminate employees for "good cause," which will be defined differently in each jurisdiction. In addition, some states prohibit the termination of an employee "in violation of public policy."[92] Finally, certain aspects of employees' collective bargaining agreements, if applicable, may be relevant. The company should be aware of the applicable law in the relevant jurisdiction, as well as its contractual obligations, prior to acting.

Discipline for Underlying Conduct Uncovered During an Investigation

If facts come to light during an investigation that indicate that there was misconduct, whether intentional or not, by an employee or employees of the company, it is essential that that information be conveyed immediately to the client or appropriate personnel at the company. If the misconduct is ongoing, action should be taken to stop it. In addition to the obvious benefit of halting the inappropriate behavior or practices, taking immediate action can serve as a signal to regulators and law enforcement, as well as the investment community, that the company is taking its obligations seriously, is operating in good faith and is willing to take difficult actions if necessary.

Despite these advantages, there are also drawbacks to acting swiftly in these situations. With respect to the conduct of the investigation itself, disciplining an employee will make it less likely that an employee will cooperate fully with the continuing investigation. If the employee is terminated, the company may lose all access to that employee, and thereby short-circuit completely at least that aspect of the investigation. For these reasons, the company should endeavor to obtain as much information as possible from such employees prior to undertaking any disciplinary action.

The company must also be cognizant of the risks of acting prior to the completion of the fact-finding portion of the investigation. While certain conduct may initially appear to warrant a sanction, facts developed later may mitigate or excuse the conduct or actions at issue. In such instances, the company may face liability to the disciplined employee for acting too hastily. Thus, it is often advisable to wait until the investigation has made significant progress prior to taking any action. In addition, if at all feasible (i.e., in any non-emergency situation), employees should be provided an opportunity to respond, formally or informally, prior to any action being taken against them. This will allow the investigation to obtain more facts, while simultaneously helping to insulate the company from any claim that it acted unfairly.

Any disciplinary action taken in the midst of an investigation may also alert the SEC, other law enforcement or potential third party litigants of possible wrongdoing. It is not uncommon, especially in the heavily-regulated securities industries, for employee discipline to lead to a formal or informal inquiry by the SEC into the circumstances underlying the company's actions. The company must be prepared to face scrutiny at that time not only about the decision to discipline the employee, but also about the underlying facts and circumstances that prompted the investigation in the first place.

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[92] Specifically, courts have recognized that at least "at will" employees may have a common law cause of action against their employer in such circumstances. *See, e.g., Edmondson v. Shearer Lumber Prods.*, 75 P.3d 733 (Id. 2003); *Porterfield v. Mascari II, Inc.*, 823 A.2d 590 (Md. 2003); *Little v. Auto Stigler, Inc.*, 63 P.3d 979 (Cal. 2003).

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