

**RESOLUTION ADOPTED BY THE
HOUSE OF DELEGATES
OF THE
AMERICAN BAR ASSOCIATION
AUGUST 2004***

RECOMMENDATION

RESOLVED, THAT the American Bar Association urges the United States Congress to make the following changes to the proposed amendments to the Sentencing Guidelines for Organizations:

1) Amend the Application Note to § 8C2.5 to state affirmatively that waiver of the attorney-client privilege and work product protection should not be a factor in determining whether a sentencing reduction is warranted for cooperation with the government.

2) Retain the approach of the 1991 Sentencing Guidelines to determine whether a compliance program is effective, or create a sliding scale for reductions in an organization's culpability score based on the degree to which an organization satisfies the various criteria in proposed § 8B2.1;

3) Amend proposed § 8C2.5(f)(2) to provide: "Subsection (f)(1) shall not apply if, after becoming aware of an offense, the organization unreasonably delayed (a) in taking appropriate steps to terminate any continuing unlawful conduct, or (b) in assessing whether the organization's compliance program should be modified in light of the discovery of the offense, and thereafter implementing any appropriate modifications; "

4) Amend proposed § 8C2.5(f)(3) to: (a) eliminate any absolute unavailability of a culpability score reduction if high-level personnel participated in, condoned, or were willfully ignorant of the violation; and (b) establish a rebuttable presumption that an organization's compliance program was ineffective if personnel at the officer or executive level participated in, condoned, or were willfully ignorant of the violation; and

5) Insert an Application Note stating that if an organization conducts an assessment annually, and promptly after the discovery of any criminal offense committed by a member of the organization, the organization has conducted the periodic assessments required by proposed § 8B2.1(c) with sufficient frequency.

*Note: The "Recommendation," but not the attached "Report," constitutes official ABA policy.

REPORT

On April 30, 2004, the United States Sentencing Commission transmitted to Congress proposed amendments to the United States Sentencing Guidelines.¹ The amendments – the first substantial revision since the Guidelines became effective in 1991 – will become effective on November 1, 2004, unless Congress takes affirmative action.

The Supreme Court's intervening decision in *Blakely v. Washington*² casts doubt on the constitutionality of the Sentencing Guidelines, and lower federal courts have already split on *Blakely's* application to the Guidelines. This recommendation takes no position on the controversy, although its supporters join Congress in calling on the Supreme Court to decide the matter expeditiously and note with approval the Supreme Court's recent grant of petitions for writs of certiorari to review these important issues.³

This recommendation addresses two concerns that will remain important regardless of how the *Blakely* issues are resolved.

First, the recommendation criticizes the implicit requirement that organizations waive the attorney-client privilege and work product protections in order to demonstrate “thorough” cooperation with the government and thereby qualify for a reduction in the culpability score under the Guidelines.

Second, the recommendation addresses several troubling revisions to the factors a court should consider in determining whether a compliance program is “effective.” Certain proposed changes introduce an “all or nothing” evaluation of effectiveness, including: (1) the requirement that the organization promptly report violations to the government or lose all credit for its compliance program; and (2) the automatic prohibition of a downward departure for an effective compliance program if high-level personnel were involved in the violation. Problems with other provisions could lead to arbitrary and disparate application of the Guidelines, including: (1) lack of clarity as to the process to be used to assess whether a compliance program is “effective”; (2) lack of guidance as to the meaning of “assess the risk of criminal conduct”; and (3) subjectivity inherent in the requirement that the program “promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law.”

I. WAIVER OF ATTORNEY-CLIENT PRIVILEGE SHOULD NOT BE A FACTOR IN ASSESSING AN ORGANIZATION'S COOPERATION.

The Sentencing Commission's proposed requirement that an organization waive the attorney-client privilege and work product protection in at least some situations in order to demonstrate cooperation with the government will undermine fundamental principles of the American legal system and reduce the effectiveness of corporate programs intended to prevent

¹ The full text of the proposed amendments was published in the Federal Register on May 19, 2004. 69 Fed. Reg. 28994-29028.

² 542 U.S. ___, 72 USLW 4546 (June 24, 2004).

³ *United States v. Booker* (No. 04-104); *United States v. Fanfan* (No. 04-105)(cert. granted August 2, 2004).

and detect criminal conduct. This will retard rather than advance compliance – one of the core objectives of the Organizational Sentencing Guidelines. This recommendation asks Congress to insist that the Guidelines include an affirmative statement that a reduction for cooperation does not require waiver of these fundamental protections for effective representation.

A. The Proposed Amendment

The proposed amendment to Application Note 12 relates to Section 8C2.5(g), which governs a reduction in culpability score for an organization’s self reporting, cooperation, and acceptance of responsibility. Application Note 12 currently provides that cooperation with the government’s investigation must be “timely and thorough,” which includes:

...the disclosure of all pertinent information known by the organization. A prime test of whether the organization has disclosed all pertinent information is whether the information is sufficient for law enforcement personnel to identify the nature and extent of the offense and the individual(s) responsible for the criminal conduct.

The proposed amendment adds the following sentence:

Waiver of attorney-client privilege and of work product protections is not a prerequisite to a reduction in culpability score under subdivisions (1) and (2) of subsection (g) *unless such waiver is necessary in order to provide timely and thorough disclosure of all pertinent information known to the organization.* (Emphasis added.)

The proposed amendment singles out attorney-client and attorney work product information. . No standards are suggested for when such a waiver will be “necessary,” nor does the proposal address the potential procedural morass of a post-hoc judicial determination of such necessity.

B. Attorney-Client and Work Product Protections Are Crucial to Effective Legal Representation and Fundamental to the Adversary System

The United States Supreme Court has stated:

The attorney-client privilege is the oldest of the privileges for confidential communications known to the common law Its purpose is to encourage full and frank communications between attorneys and their clients and thereby promote broader public interests in the observance of law and administration of justice.⁴

The Court has rebuffed attempts to narrow the privilege for corporations; to do so would:

not only make it difficult for corporate attorneys to formulate sound advice when their client is faced with a specific legal problem but also threaten to limit the valuable efforts of corporate counsel to ensure their client’s compliance with the law.⁵

The privilege is vital to encourage “the communication of relevant information by employees of

⁴ *Upjohn Co. v. United States*, 449 U.S. 383, 389 (1981).

⁵ *Id.* at 392.

the client to attorneys seeking to render legal advice to the client corporation.”⁶

Moreover, effective legal representation requires that the attorney-client privilege be certain. The Supreme Court explained:

If the purpose of the attorney-client privilege is to be served, the attorney and client must be able to predict with some degree of certainty whether particular discussions will be protected. An uncertain privilege, or one which purports to be certain but results in widely varying applications by the courts, is little better than no privilege at all.⁷

The Supreme Court concluded that withdrawal of the protection cannot be justified by case-by-case expediency. The privilege has been sustained repeatedly against arguments that it impedes finding the truth. Courts instead stress that the privilege promotes a “public goal transcending the normally predominant principle of utilizing all rational means for ascertaining truth.”⁸

The attorney work product protection is also recognized as a crucial component of our system of justice. The Supreme Court explained that the doctrine promotes the adversary system by enabling attorneys to prepare cases without fear that their work product will be used against their clients, and that it affords “a certain degree of privacy” to discourage “unfairness.”⁹

C. Recent Department of Justice Policy Has Eroded These Fundamental Attorney-Client Protections

Despite unequivocal judicial support of principles protecting attorney information, the Department of Justice (“DOJ”) has pursued a policy that reduces their certainty and utility. The Sentencing Commission’s proposed amendment embraces and extends this misguided policy.

The government has sought voluntary disclosure of information from corporations for many years. During the early 1980s, the government sought disclosure from corporations being investigated for fraud on the Department of Defense.¹⁰ The leniency program of the Antitrust Division of the DOJ also relies on voluntary disclosure.¹¹ The leniency program has produced the most important antitrust convictions of the last decade, including the largest criminal fine in the nation’s history.¹² Neither the Defense or Antitrust Division programs, however, sought waiver of the attorney-client or work product protections.

The waiver of these protections was introduced in a June 1999 DOJ memorandum entitled “Federal Prosecution of Corporations,” known as the “Holder Memorandum.” It

⁶ *Id.* at 392.

⁷ *Upjohn Co. v. United States*, *supra* at 393.

⁸ *Trammel v. United States*, 445 U.S. 40, 50 (1980).

⁹ *Hickman v. Taylor*, 329 U.S. 495, 510-11 (1947).

¹⁰ Public hearing held by the Ad Hoc Advisory Group on Organizational Sentencing Guidelines, Nov. 14, 2002, at 122.

¹¹ *Id.* at 35.

¹² Scott D. Hammond, *A Review of Recent Cases and Developments in the Antitrust Division’s Criminal Enforcement Program*, at 3 (2002).

encouraged seeking waivers in determining whether to bring charges. It states:

In gauging the extent of the corporation's cooperation, the prosecutor may consider the corporation's willingness to identify the culprits within the corporation, including senior executives, to make witnesses available, to disclose the complete results of its internal investigation, and to waive attorney-client and work product privileges.

The Holder Memorandum stated that waiver was not an absolute requirement, but nevertheless was a factor to consider in evaluating the corporation's cooperation. It relied on the prosecutor's discretion to determine whether waiver necessary in the particular case.

The waiver policy was expanded in a January 2003 memorandum entitled "Principles of Federal Prosecution of Business Organizations" by Deputy Attorney General Larry Thompson:

One factor the prosecutor may weigh in assessing the adequacy of the corporation's cooperation is the completeness of its disclosure including, if necessary, a waiver of the attorney-client and work product protection, both with respect to its internal investigation and with respect to communications between specific officers, directors, and employees and counsel. Such waivers permit the government to obtain statements of possible witnesses, subjects and targets without having to negotiate individual cooperation or immunity agreements. In addition, they are often critical in enabling the government to evaluate the completeness of a corporation's voluntary disclosure and cooperation. Prosecutors may, therefore, request a waiver in appropriate circumstances. The Department does not, however, consider waiver of a corporation's attorney-client and work product protection an absolute requirement, and prosecutors should consider the willingness of a corporation to waive such protection when necessary to provide timely and complete information as one factor in evaluating the corporation's cooperation.¹³

Both the Holder Memorandum and the Thompson Memorandum state that waiver is not mandatory and should not be required in every situation. This concept also was included in the Sentencing Commission's proposal. The practical effect of this concept, however, is troubling. It appears that the government frequently demands waiver of privilege and disclosure of protected information. Moreover, disclosure is demanded at the very beginning of the investigation, even before the government has sought to obtain information through techniques such as grand jury subpoenas, warrants, and in appropriate circumstances, compulsion of testimony.¹⁴ The U.S. Attorney for the Southern District of New York "has publicly called for a complete waiver of the attorney-client privilege by all corporate targets wishing to obtain credit for their cooperation."¹⁵

The combination of DOJ's policy and the Sentencing Commission's proposal will result

¹³ Memorandum from Larry D. Thompson, Deputy Attorney General, Department of Justice, to Heads of Department Components, U.S. Attorneys, Principles of Federal Prosecution of Business Organizations (January 20, 2003), available at www.usdoj.gov/dag/cftf/corporate_guidelines.htm.

¹⁴ Public hearing held by the Ad Hoc Advisory Group on Organizational Sentencing Guidelines, *supra*, at 27.

¹⁵ Judson W. Starr and Brian L. Flack, *Government's Insistence on a Waiver of Privilege*, WHITE COLLAR CRIME 2001 J-1, at J-4 (ABA 2001).

in a demand for waiver in nearly all situations. The government will be able to determine when waiver and disclosure are “necessary” for “thorough” cooperation, and targeted or defendant corporations will be unable to counter that assertion effectively. This will lead inevitably to the elimination of these protections for corporations that attract the government’s attention. Judicial determinations of the importance of these protections will be effectively circumvented by executive branch policy and Sentencing Commission determination –without any considered congressional review.

D. Waiver of the Attorney-Client Privilege and Work Product Protections Will Undermine Counseling, Compliance, and Detection.

1. Employee candor will be greatly compromised by the waiver requirement.

Counsel customarily interview employees to determine the existence and extent of corporate wrongdoing. Employee candor is essential for any effective internal investigation or compliance program. Requiring an organization to waive its attorney-client privilege in order to seek a sentence reduction will discourage employees to be candid. If they believe their statements will be turned over to the government, they are not likely to be frank with counsel.

This disincentive will change the dynamic of the counsel-client-employee relationship. First, if employees are not candid and forthcoming, counsel will be required to formulate legal advice to the client without full and complete information.

Second, if employees agree to meet with company counsel, they will be far more likely to seek or separate counsel to protect their personal interests. Individual counsel often advise the employee to share information with the company’s counsel only under a joint defense relationship, under which the information will be privileged as to both the organization and the individual, and the organization will be prohibited from disclosing the information to the government without the individual’s consent. Corporate cooperation with the government will become more difficult and cumbersome, serving neither’s interest.

Third, waiver undermines the policy of full and frank internal disclosure of corporate wrongdoing espoused by the Sarbanes-Oxley Reform Act of 2002. The Act encourages, and in some cases requires employees (and their counsel) to report corporate wrongdoing “up the ladder.”¹⁶ Waiver of attorney-client privilege will discourage employees from reporting possible violations because what they report may subject them to investigation and prosecution.

Fourth, recent prosecutorial trends may soon place employees in the untenable position of having to choose between disclosing information to counsel that could lead to their prosecution or staying silent and losing their jobs. In a recent securities matter, employees were prosecuted for obstructing justice because they lied to outside counsel who disclosed their statements in an effort to cooperate fully with the government.¹⁷ This raises the same concerns underlying the

¹⁶ 18 U.S.C. §1514A. This provision makes it illegal for a company that has a class of securities registered under Securities Exchange Act of 1934 or otherwise has to file reports under that act to retaliate against any employee who reports information to a supervisor, a regulatory or law enforcement agency or Congress.

¹⁷ See e.g., Alex Berenson, *Case Expands Type of Lies Prosecutors Will Pursue*, N.Y. TIMES, MAY 17, 2004, at

constitutional privilege against self-incrimination. The Supreme Court has written that the Fifth Amendment privilege avoids subjecting individuals to the “cruel trilemma” of self-incrimination, perjury, or contempt.¹⁸ A policy promoting waiver of these privileges will subject employees to the cruel trilemma of self-accusation, obstruction of justice or discharge.¹⁹

Last, the waiver policy raises ethical issues for counsel conducting internal investigations. Rule 4.3 of the Model Rules of Professional Conduct provides that an organization must retain separate counsel for an employee when it realizes that the individual’s interest has become adverse to the organization.²⁰ An anticipated waiver of the attorney-client privilege could establish at the outset that the organization’s interests are adverse to the individual. At minimum, corporate counsel may have to warn employees that their statements may be disclosed to the government and may be used against them. After such a *Miranda*-type warning, employees likely will refuse to be interviewed or will be less than forthcoming.

2. Organizations may not be able to qualify for a fine reduction for implementing an “Effective Compliance” program.

The waiver provisions will also reduce an organization’s ability to obtain a sentence reduction for an “effective compliance” program. One of the Sentencing Commission’s proposed amendments encourages corporations to engage in effective compliance and improve general business ethics. Allowing prosecutors to require privilege waiver to meet the requirements for “full cooperation” will hinder the organization’s ability to take effective, meaningful steps to fulfill this important mission.

According to the proposed amendment, in an “effective compliance and ethics program” the organization “exercise[s] due diligence to prevent and detect criminal conduct; and otherwise promote an organization culture that encourages ethical conduct and a commitment to compliance with the law.”²¹ The program “shall be reasonably designed so that it is generally effective in preventing and detecting criminal conduct.”²² Most corporate crimes are detected through the admissions of employees. If an organization’s employees are unwilling to be candid for fear that their statements will be produced to the government, counsel will not be as effective in detecting and investigating corporate misconduct.

Although the Guidelines are not specific about the due diligence required in detecting and preventing crime in order to constitute “effective compliance,” lack of employee candor undoubtedly undermines that goal. In analyzing whether to establish and pursue a compliance program, the costs of compliance and the threat of civil exposure might outweigh any benefit from voluntary disclosure unless there is a realistic chance of reducing exposure.

C1.

¹⁸ *Murphy v. Waterfront Commission*, 378 U.S. 52, 55 (1964).

¹⁹ The Department of Justice has stated in its Criminal Resource Manual, Art. 162, §VI.B:

Such waivers permit the government to obtain statements of possible witnesses, subjects, and targets, without having to negotiate individual cooperation or immunity agreements.

²⁰ See MODEL RULES OF PROF’L CONDUCT R. 1.6, 1.13 (Comment 10), and 4.3.

²¹ See PROPOSED AMENDMENTS TO THE U.S. SENTENCING GUIDELINES §8B2.1.

²² *Id.*

E. Waiver Will Promote Private Civil Litigation and Diminish Corporate Self-Reporting

If an organization waives the attorney-client and work product protections to try to reduce its criminal penalty, the number of civil lawsuits will increase dramatically. Potentially ruinous claims will be generated under the numerous statutes that provide for treble damages and in some instances threaten duplicate recovery by multiple plaintiffs. This increase in civil liability will directly affect the cost-benefit analysis in deciding whether to self-report a potential criminal violation. In many situations, an organization may decide that the risk of increased civil liability outweighs the uncertain benefit of a lower criminal fine.

Waiver of these protections to cooperate with the government will also mean that civil litigants gain access to privileged information. Once an organization discloses privileged information to the government it is discoverable by all civil litigants.²³ Even in jurisdictions where complete waiver of the privilege is not automatic, courts often will engage in a case-by-case analysis of the intended scope of the waiver and order disclosure of privileged information.²⁴ Because an organization will not know the full scope of the waiver when it decides to cooperate with the government, it must assume the privilege will be waived with respect to all potential parties.²⁵

Privileged communications and attorney work product created during an internal investigation are extremely valuable to private plaintiffs. Knowing that reports of those investigations provide a virtual blueprint for their suits, plaintiffs aggressively seek production in discovery. Companies faced with the possibility of increased civil liability may choose instead not to self-report violations or decline to cooperate with the government.

A decline in such disclosure will reduce the number of prosecutions. The Antitrust Division, for example, relies on self-reporting and its corporate leniency program to generate many of its criminal cases. According to two top Antitrust Division officials, the “majority of the Division’s major international investigations have been advanced through the cooperation of an amnesty applicant.”²⁶ Between October 2002 and March 2003, three corporations applied for amnesty each month.²⁷ Amnesty applications have resulted in \$1.5 billion in fines, or three-quarters of the total fines obtained by the Antitrust Division, since 1997.²⁸

²³ See, e.g., *In re Columbia/HCA Healthcare*, 293 F.3d 289, 298-302 (6th Cir. 2002); *United States v. Massachusetts Institute of Technology*, 129 F.3d 681 (1st Cir. 1997); *Westinghouse Electric Corp. v. Republic of the Philippines*, 951 F.2d 1414 (3d Cir. 1991); *In re Martin Marietta Corp.*, 856 F.2d 619 (4th Cir. 1988); *Permian Corp. v. United States*, 665 F.2d 1 (D.C. Cir. 1981).

²⁴ *In re Steinhardt Partners L.P.*, 9 F.3d 230, 236 (2d Cir. 1993).

²⁵ In an investigation relating to potential international conduct, a waiver could have effects in foreign countries that are difficult or impossible to assess.

²⁶ James M. Griffin & Scott D. Hammond, *An Overview of Recent Developments in the Antitrust Division’s Criminal Enforcement Program*, at 8-9 (2003).

²⁷ Gary R. Spratling & D. Jarrett Arp, *The International Leniency Revolution: The Transformation of International Cartel Enforcement During the First Ten Years of the United States’ 1993 Corporate Amnesty/Immunity Policy*, at 9 (2003)

²⁸ *Id.* at 12-13.

Clearly the government relies heavily on the voluntary disclosure of potential corporate misconduct. An incentive structure that dissuades companies from coming forward will hurt the government's efforts to detect and prosecute criminal violations and eventually reduce compensation to victims either through the restitution provisions of criminal law or civil litigation.²⁹ While obtaining privileged information may seem advantageous to the government and to civil litigants in a particular case, waiver and forced disclosure will prove disadvantageous to long-run enforcement policy.³⁰

F. Implementation of the Proposed Amendment Will Generate Significant Procedural Issues.

The proposed amendment to Application Note 12 requires a waiver whenever "such waiver is necessary in order to provide timely and thorough disclosure of all pertinent information known to the corporation." The broad language will allow the government to argue that a waiver is required whenever, in its view, information could be provided faster or more fully through a waiver than without one.

This "exception" will swallow the rule. In the aftermath of an internal investigation, whether the company has decided to self-report or has come under suspicion through other means, the government will know more, and more quickly, if the company discloses its protected information. Internal investigations regularly reveal information about the methods and means through which crimes were committed, identify culpable parties, and provide information about potential civil damages to the corporation and its shareholders, creditors or others. The attorneys, investigators and accountants conducting such investigations often present these findings through oral and written reports to the company. This information, if conveyed to the government, would certainly advance nearly every government investigation.

While some claims of "necessity" may fall under the glare of judicial scrutiny, many will never be litigated because of the extreme risks to the company. In a particular matter, the government may have an insufficient basis to argue "necessity," but its threat to raise that issue in court – which will taint the company as being noncooperative – will have a profound impact on the company, including its stock price and credit worthiness. Few companies will risk such litigation. Rather, the company is likely to waive its privilege if the prosecutor threatens to litigate the issue, placing such cases beyond the scrutiny of the judiciary and greatly enhancing the government's coercive power over the organization under investigation.

Even if litigated, the proposed amendment invites selective application by the government. If the government contends that a waiver was "necessary," and therefore that

²⁹ A guilty plea to an antitrust conspiracy constitutes *prima facie* evidence of a violation for civil damage plaintiffs. 15 U.S.C. § 16(a).

³⁰ The Antitrust Division has concluded that privilege waiver is not necessary for effective prosecution. Presumably, this is because the first corporation to invoke the Corporate Leniency Policy must "report[] the wrongdoing with candor and completeness and provide full, continuing and complete cooperation to the Division throughout the investigation," thereby negating the need to require waiver. See <http://www.usdoj.gov/atr/public/guidelines/0091.htm>. Armed with the information gleaned from the first leniency applicant, the Division can exert pressure to obtain the relevant facts and pleas from others involved in the conspiracy.

cooperation credit should be denied, a corporate defendant will be entitled to discovery and a hearing concerning the progress of the investigation from its inception to determine whether a waiver was truly “necessary.” If aspects of the investigation are confidential, or the government believes disclosure of investigative techniques will be detrimental, it may avoid the litigation by refraining from raising the issue. However, in cases with no confidentiality concerns, the government may choose to litigate. Thus, two companies in similar circumstances, who provided equal cooperation, could be treated differently depending on the government’s view of the collateral consequences rather than on the merits.

II. CERTAIN PROVISIONS OF THE SENTENCING GUIDELINES DIMINISH THE INCENTIVES FOR VIGOROUS AND EFFECTIVE COMPLIANCE PROGRAMS

A. Proposed §8C2.5(f)(2) Diminishes The Incentives For Organizations To Implement Compliance Programs.

Under current § 8C2.5(f), an organization must not “unreasonably [delay] reporting the offense to appropriate governmental authorities,” otherwise, it forfeits the culpability score reduction. This requirement undermines rather than promotes compliance programs. Organizations that adopt and implement even the most effective compliance programs are still likely to discover occasionally that an employee has violated the law. At that time, and regardless of the organization’s commitment to deterring violations, management must consider a variety of issues when deciding whether to report to the government, and may reasonably conclude that the organization is best served by non-disclosure. In deciding how the organization should respond, management’s fiduciary duty requires a decision that best serves the interests of the organization and its shareholders or creditors.³¹ The organization may select a course of action other than prompt self-reporting.

For example, the organization may decide to delay self-reporting to investigate the scope of the behavior. Time might be needed to evaluate the potential damage to its reputation and the financial repercussions of revealing the violation. The organization might conclude that early self-reporting in one jurisdiction is likely to increase the organization’s risk of prosecution in other jurisdictions, and therefore is not in the organization’s overall best interest. In some cases, there might be very little risk of criminal prosecution but a possibility of huge civil liability.

Proposed § 8C2.5(f)(2), however, would deny any credit for even the most comprehensive and effective compliance program if the organization determines that its best interests are served by a course of action that does not include prompt self-reporting. The culpability score reduction is eliminated regardless of whether the organization’s compliance program was effective in detecting violations. Thus, proposed § 8C2.5(f)(2) conflates two separate concepts – implementation of an effective compliance program, and increasing the efficiency and timeliness of law enforcement through self-reporting.

These two concepts should not be linked, particularly since the Guidelines already provide a powerful incentive for organizations to self-report: § 8C2.5(g) offers a five point culpability score reduction. An organization’s reporting decision may not relate to whether it

³¹ See, e.g., *Smith v. van Gorkom*, 488 A. 2d 858, 872 (Del. 1985).

operates an “effective compliance program,” but rather to whether the organization believes an appropriate resolution can be achieved without the intervention of the government. Regardless of the reason for the decision to refrain from disclosure, if the organization terminates the illegal conduct, the deterrence sought by the Guidelines has been largely achieved.

Accordingly, proposed § 8C2.5(f)(2) should be revised to provide that “Subsection (f)(1) shall not apply if, after becoming aware of an offense, the organization unreasonably delayed (a) in taking appropriate steps to terminate any continuing unlawful conduct, or (b) in assessing whether the organization’s compliance program should be modified in light of the discovery of the offense, and thereafter implementing any appropriate modifications.” These changes would tie the availability of the culpability score reduction to the goals of a compliance program — deterrence of crime through education and oversight.

B. Proposed §8C2.5(f)(3) Diminishes The Incentives For Organizations To Implement Compliance Programs.

Section 8C2.5(f) contains a rebuttable presumption that an organization’s compliance program was not effective, and therefore that the organization’s culpability score should not be reduced, if high-level personnel participated in the offense. The involvement of some high-level personnel in a violation does not necessarily mean that the organization’s compliance program was ineffective at deterring others. The overall effectiveness of the program should be analyzed. By conjoining two issues that should be distinct – the creation of an effective compliance program and the involvement of high-level personnel in a particular offense – proposed § 8C2.5(f)(3) reduces the incentives for organizations to create meaningful compliance programs.

Organizations are likely to perceive proposed § 8C2.5(f)(3) as an empty promise. Although the Guidelines hold out the possibility that an organization might rebut the presumption that its program was ineffective, few organizations are likely to view this as a realistic possibility.

This is an inappropriately high standard. First, “high-level personnel” includes a much broader range of employees than was likely intended to be covered by this provision. Second, it cannot be expected, particularly for larger organizations, that even the most comprehensive compliance program will always deter every possible violation by every “high-level” employee. Third, the benefits of giving organizations incentives to devote attention and resources to compliance programs are significant enough that the Guidelines should not decrease those incentives. Indeed, “high-level employees” are likely to be in the position to commit the worst, and most harmful, crimes. Recognizing that even the most diligent organization cannot be assured of deterring every possible violation by a “high-level employee,” while still creating incentives for organizations to deter this potential misconduct, will benefit society significantly.

Accordingly, the Guidelines should adopt a three-tiered approach that would maintain, and even enhance, the incentive for an effective compliance program. Specifically, if the violation included the Chief Executive Officer, Chief Financial Officer, Chief Operating Officer, or Chief Legal Officer, the organization should be required to rebut the presumption that the compliance program was not effective. This would require a clear showing that the governing body exercised substantial oversight of the offending employee(s), which was frustrated by

efforts to conceal their criminal conduct. If one or more other officers or executives were involved, the presumption that the organization's compliance program was not effective could be rebutted by a showing that the program was generally effective at deterring criminal violations by employees (including "high-level" employees) not involved in the conduct being prosecuted. Finally, if the violation involved "high-level employees," but officer and executive level employees were not involved in, did not condone and were not willfully ignorant of the violation, there would be no presumption, and the program would be reviewed under the amended § 8B2.1.

C. Proposed §§8B2.1(a), (b), and (c) Diminish The Incentives For Organizations To Implement Compliance Programs.

The Guidelines need more certainty in describing an effective compliance program. The proposed amendments, however, go too far by requiring that organizations "exercise due diligence to prevent and detect criminal conduct," "otherwise promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law," and "periodically assess the risk of criminal conduct and ... take appropriate steps ... to reduce the risk of criminal conduct...." Proposed §§8B2.1(a)-(c). These proposals convert useful and valuable guidance on current best practices for effective compliance programs into a laundry list of mandatory minimums, each of which is a prerequisite to *any* reduction in the organization's culpability score.

Unfortunately, organizations are likely to view proposed § 8B2.1 as setting an unobtainable standard. This is a significant change from the 1991 Guidelines, which, instead of establishing specific criteria that compliance programs would be required to meet, outlined seven "types of steps" that organizations should take to develop and maintain effective compliance programs.³² The 1991 approach provided guidance while acknowledging that the elements of effective compliance programs can vary. This approach reflected the practical reality that organizations may develop compliance programs that differ in priorities and design, based on specific industry characteristics and circumstances.

Proposed § 8B2.1 transforms guidance into a series of mandatory minimum requirements, including the seven separately-enumerated provisions of § 8B2.1(b), and at least two additional requirements in §§ 8B2.1(a)(2) and 8B2.1(c). Indeed, because several subsections contain multiple obligations, it appears that an organization's compliance program would have to meet over twenty discrete requirements before reduction in culpability score would be warranted. By creating so many hurdles, and by providing that the failure to meet any one standard is fatal, the amendments leave the impression that an organization's prospects for a tangible benefit are remote or, at best, inherently uncertain. The amendments will cause organizations to conclude that sentencing reduction will not be conferred, and thus diminish the incentive for implementation.

This problem is exacerbated by the vague and ambiguous language of the proposed amendment. For example, proposed § 8B2.1(a)(2) requires organizations to "otherwise promote an organizational culture that encourages ethical conduct and a commitment to compliance with

³² § 8A1.2, cmt.3(k).

the law.” While this provision describes desirable attributes of an effective compliance program, it is too subjective to be applied with uniformity by the judiciary and contravenes one of the central aims of the Guidelines, avoidance of unwarranted sentencing disparities.³³

Varying judgments by prosecutors and courts concerning what constitutes “ethical conduct” and what is an acceptable “organizational culture” are inevitable. These are areas best left to the judgment of the leadership of the organization and should not be second guessed in hindsight by the courts.³⁴ Indeed, the Advisory Group recognized the dangers in imposing such a requirement:

It is also intended to avoid requiring prosecutors to litigate and judges to determine whether an organization has a good “set of values” or appropriate “ethical standards,” subjects which are very difficult, if not impossible, to evaluate in an objective, consistent manner.³⁵

Accordingly, the “organizational culture” provision of § 8B2.1 be deleted. Instead, an Application Note should be inserted acknowledging that in most instances an effective compliance program will promote an organizational culture that encourages ethical conduct and compliance with the law. To afford the greatest degree of latitude to management, a court should be hesitant to conclude that a compliance program was ineffective because of the organization’s “culture,” except where the program was a sham or a culture of disregard for the law was promoted.

The requirement of proposed § 8B2.1(c) is similar. It requires that an organization “periodically assess the risk of criminal conduct” and “take appropriate steps to design, implement, or modify each requirement set forth in [proposed § 8B2.1(b)] to reduce the risk of criminal conduct identified through the process” described in proposed § 8B2.1(b). Although Application Note 6 to proposed § 8B2.1 provides some additional guidance as to the factors that organizations should review, it does not specify how frequently or comprehensively the assessment must be conducted to meet the requirement.

While programs can become so outdated that they are ineffective, it is unfair to deprive an organization of any sentencing benefit because of the failure to perform the required periodic assessment. To resolve these concerns, and avoid inevitably subjective prosecutorial judgments, an Application Note should be included. The Note should provide that an assessment is sufficient if it was conducted on an annual basis and promptly after the discovery of misconduct, in the absence of evidence that the assessment was a sham.

Similarly, the various subsections of § 8B2.1(b) impose vague requirements that invite disputes between organizations and the government. For example, § 8B2.1(b)(2)(A) requires that the organization’s governing authority must “exercise reasonable oversight” over the

³³ 28 U.S.C. § 991(b)(1).

³⁴ *Cf. Aronson v. Lewis*, 473 A.2d 805 (Del. 1984), overruled on other grounds, *Brehm v. Eisner*, 746 A.2d 244 (Del. 2000). *Aronson* sets out the business judgment rule as “a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company.” *Id.*

³⁵ See Ad Hoc Advisory Group Report, at 58, available at <<http://www.ussc.gov/corp/advgrprpt/advgrprpt.htm>>.

compliance program, but no standards are described.³⁶ The same concern applies to the requirements that: the individuals who are given operational responsibilities for the compliance program must have “adequate” resources and “appropriate” authority;³⁷ the organization must use “reasonable” efforts not to include in its substantial authority personnel any individuals who have engaged in criminal activities in the past;³⁸ the organization must take “reasonable” steps to communicate its compliance standards and procedures “periodically and in a practical manner,” and conduct “effective” training;³⁹ the organization must take “reasonable” steps to ensure compliance with the program, to evaluate periodically its “effectiveness,” and to “publicize” a reporting system;⁴⁰ and the compliance program must be promoted and enforced “consistently” throughout the organization through “appropriate” incentives and disciplinary measures.⁴¹

Organizations may perceive these vague requirements as setting an unreasonably high standard. This is particularly important since the organization would be required to prove that every one of these requirements was fulfilled, most likely by a preponderance of the evidence.⁴² Raising the bar so high effectively means that few organizations will receive a culpability score reduction. The carrot-and-stick approach described by the Ad Hoc Advisory Group to the Sentencing Commission would no longer include a carrot. This is not only unfair, but likely to eliminate the sentencing reduction as a factor in an organization’s decision to create and implement a compliance program.

The current approach allows courts to assess an organization’s efforts and decide whether they have been sufficiently vigorous to deserve a sentencing reduction. This approach should be retained instead of the mandatory minimum criteria reflected by the proposed amendments. This approach provides a strong incentive while permitting courts to evaluate whether organizations have demonstrated a sincere and vigorous commitment to compliance with the law.

³⁶ See § 8B.21(b)(1)(A).

³⁷ § 8B.21(b)(2)(C).

³⁸ § 8B.21(b)(3).

³⁹ § 8B.21(b)(4)(B).

⁴⁰ § 8B.21(b)(5).

⁴¹ §§ 8B.21(b)(6) and (7).

⁴² See *United States v. Anderson*, 259 F.3d 853, 858 (7th Cir. 2001).