From Advancement Rights to Upjohn Warnings
The Ethics of Internal Investigations

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Part I

INVESTIGATION BASICS

Regulatory Expectations

- Entities are to self-police.
- Self-policing begins with an independent compliance function, including:
  - Policies, controls and procedures
  - Training
  - Compliance audits
  - Assessment, monitoring and follow-up
- When issues are identified, investigate.

Common Sources

- Issues for investigation commonly arise from:
  - Exit interviews & performance evaluations
  - Hotline complaints
  - Competitor allegations
  - Whistleblower complaints
  - Lawsuits
  - Law enforcement inquiries

Benefits of Internal Investigations

- Rapid fact finding in an environment protected by the attorney-client and work product privileges;
- Critical to securing cooperation credit, including:
  - Reduction in fines;
  - Reduction in defense costs;
  - Avoidance of criminal sanctions;
  - Reputational benefits.
- Enables deployment of proactive strategies (e.g., self-reporting, strengthening controls, public relations).
- Reduces/avoids interdepartmental conflicts.

Immediate Mitigation

- Define the issue(s).
- If an issue is ongoing, immediate steps should be considered to mitigate associated risks.

Example in the Healthcare Space:

- Is the issue systemic?
- Does the issue impact billing and/or reimbursement?
  - Directly – i.e., systemic issue impacting coding?
  - Indirectly – i.e., impacting meaningful use incentives?
- If the issue is ongoing or if it is uncertain, consider putting a short term billing hold in place until the issue can be corrected or confirmed not ongoing
- Document hold

Who Should Conduct the Investigation?

Advantages to In-House Counsel:

- Familiar with company structure, products, customer base and personnel;
- Faster access to information;
- More cost advantageous.

Advantages to Outside Counsel:

- Independent;
- Greater resources and specialized knowledge;
- Stronger privilege protections;
- Avoid conflicts with internal stakeholders.

The Big Question: Investigation Scope

- How much is enough? Prevent the “runaway” investigation with a short leash.
- Consider requiring an initial written work plan with a clearly defined scope.
- Scope of work should be revisited on a periodic basis or upon reaching specified milestones.

Stay Informed When Using Outside Counsel

Rule 1.4(3) Communication with Clients

A lawyer shall:

" keep the client reasonably informed about significant developments relating to the representation, including promptly complying with reasonable requests for information and copies of significant documents when necessary to keep the client so informed."

Part II

ETHICAL CONSIDERATIONS FOR IN-HOUSE COUNSEL

The Basics

1. Your Only Client is the Organization
2. Identify and Address Conflicts Early On
3. Maintain Confidentiality and Privilege
4. Stay Informed
5. Know When and How to Report Up/Out

You Are Not Exempt

Common unsuccessful defenses raised by in-house counsel:

1. "Ethical Rules don't apply because I am in-house"

2. "I was acting as an officer of the Company, not as a lawyer"

We find nothing in the plain language . . . to suggest or even imply that lawyers who are retained by corporate clients as in-house counsel or general counsel are exempt.

Kaye v. Rosefielde, 75 A.3d 1168, 1204 (N.J. Super. Ct. App. Div. 2013); *See also People v. Miller*, 354 P.3d 1136 (Colo. O.P.D.J. 2015).

Get Licensed Where You Work

- Not being licensed where you regularly work can be a crime, an ethical violation, and destroy the claim of attorney client privilege.
  - *See, e.g.* Anwar v. Fairfield Greenwich Ltd., 982 F. Supp. 2d 260 (S.D.N.Y. 2013); *Crews v. Buckman Labs. Int'l*, 78 S.W.3d 852 (Tenn. 2002).
  - There is a split of authority on this issue.

Know Your Client

In-house counsel represents the company, not its personnel

"A lawyer employed or retained by an organization shall conform his or her representation to the concept that **the client is <u>the organization</u> itself**, acting through its duly authorized directors, officers, employees, members, shareholders, or other constituents overseeing the particular engagement." *California Rule of Professional Conduct 1.13(a) (former Rule 3-600(A))*

Ethical dilemma arises when a constituent with interests adverse to the company seeks advice on a company legal matter.

Company Personnel are Unrepresented Persons

"In communicating on behalf of a client with a person who is not represented by counsel, a lawyer **shall not state** or imply that the lawyer is **disinterested**. When the lawyer knows or reasonably should know that the unrepresented person incorrectly believes the lawyer is disinterested in the matter, the lawyer shall make reasonable efforts to **correct the misunderstanding**. If the lawyer knows or reasonably should know that the interests of the unrepresented person are in conflict with the interests of the client, the lawyer **shall not give legal advice** to that person, except that the lawyer may, but is not required to, advise the person to secure counsel."

California Rule of Professional Conduct 4.3(a) (covers latter part of former Rule 3-600(D))

Know Your Client

In certain circumstances, in-house counsel has an obligation to explain who he or she represents:

"In dealing with an **organization's constituents**, a lawyer representing the organization shall **explain the identity** of the lawyer's **client** whenever the lawyer knows or reasonably should know that the organization's **interests are adverse** to those of the constituent(s) with whom the lawyer is dealing." *California Rule of Professional Conduct 1.13(f) (former Rule 3-600(D)*

Beware of Giving Individualized Advice

- In-house counsel advises employee to "tell the truth" in a deposition: Sanctioned for giving advice to employee contrary to the employee's interest.
  - *Yanez v. Plummer,* 164 Cal. Rptr. 3d 309 (Cal Ct. App. 2013).
- In-house-counsel advised officers regarding exercise of stock options: sued by officer for malpractice.
  - *Dinger v. Allfirst Fin*., Inc., 82 Fed. Appx. 261 (3d Cir. 2003).

The Employee's Perception Controls

When is the employee acting as an extension of the company versus speaking to you as his or her personal counsel?

- "We can have a conversation in confidence, right?"
- "What I am about to tell you is only between you and me. . ."

Best practice is to clarify your role prior to receiving the information but circumstances may require advising the employee of your obligations after the fact and/or recommending separate counsel for the individual.

Rule 1.13(f)
California's "Upjohn"

In dealing with an organization's constituents, a lawyer representing the organization shall explain the identity of the lawyer's client whenever the lawyer knows or reasonably should know that the organization's interests are adverse to those of the constituent(s) with whom the lawyer is dealing.

The Elements of the "Upjohn Warning"

- Counsel represents company and not any individual employee or witness;
- Interview conducted for purpose of providing advice to company;
- Attorney-client privilege belongs solely to the company and can be waived at its discretion;
- If the company decides to waive the privilege, it may disclose the substance of the interview;
- **But** – the employee must preserve the privilege by keeping the interview confidential.

Is An Upjohn Warning Sufficient?

- Not uncommon, even after an Upjohn Warning, for employees to:
  - Ask about their personal exposure;
  - Seek personal legal advice;
  - Question whether they need separate counsel;
  - Ask questions about indemnification;
  - Inquire about their rights to decline to participate as employees.
- Questions may be posed immediately after the Upjohn Warning or much later in the interview process.

Rule 1.7
Avoiding Representation of Adverse Interests

- A member shall not, without the informed written consent of each client:

(a) represent a client if the representation is **directly adverse** to another client in the same or a separate matter; **or**

(b) represent a client if there is a **significant risk** the lawyer's representation of the client will be **materially limited** by the lawyer's responsibilities to or relationships with another client, a former client or a third person, or by the lawyer's own interests.

External Communications

"In communicating on behalf of a client with a person who is not represented by counsel, a lawyer **shall not seek to obtain** privileged or other **confidential information** the lawyer knows or reasonably should know the person may not reveal without violating a duty to another or which the lawyer is not otherwise entitled to receive." *California Rule of Professional Conduct 4.3 (covers latter part of former Rule 3-600(D))*

Subsidiaries

- Parent companies and subsidiaries are generally aligned if the subsidiaries are wholly owned and solvent.
- Subsidiaries and affiliates can generate a wide range of challenging conflict of interest and privilege issues.
  - Example: A corporation spins-off a subsidiary burdened by ongoing litigation or a regulatory investigation.
- How do the parent and subsidiary negotiate issues that will continue to impact the litigation after the spin-off, such as indemnification obligations or ownership of the attorney-client privilege?
  - See *GSI Commerce Solutions, Inc. v. BabyCenter, L.L.C., 618 F.3d 204 (2d Cir. 2010)*.

It Is Not Privileged Just Because You Heard It

Client communications must be maintained in confidence (Rule 1.6)….but client communications are not *privileged* unless (i) made for the purpose of giving or receiving legal advice and (ii) are expressed in confidence.

Test is satisfied when “one of the significant purposes” of the investigation communication was to obtain legal advice. In re Kellogg Brown & Root, Inc., 756 F.3d 754 (D.C. Cir., June 27, 2014).

The Challenges of Maintaining Privilege

- Courts may presume "business purpose" rather than "legal purpose" when an in house lawyer is included on communications.

  > "[T]he attorney-client privilege does not attach to an attorney's communications when the client's dominant purpose in retaining the attorney was something other than to provide the client with a legal opinion or legal advice." Costco Wholesale Corp. v. Superior Court, 47 Cal. 4th 725, 735 (2009).

- What this means for in-house counsel:
  - Communications between a company and its **outside counsel** almost always involve legal advice, so courts tend to apply the attorney-client privilege **broadly** to these communications
  - **In-house counsel**, however, often wear more than one hat, so courts tend to look **more closely** to analyze whether their communications with the company were for the purpose of providing legal advice or business advice

The Challenges of Maintaining Privilege

- Best Practices:
  - Mark documents as privileged and/or work product;
  - State in the document that it provides legal advice/Expressly convey the legal purpose within the document;
  - Include outside counsel on internal communications as much as possible.
  - Consider removing non-legal title from signature block.

Practice Point: Litigation Holds

- At the outset of an investigation or litigation, the number of custodians may be unclear and executives may be wary of oversharing with employees during this period of uncertainty.

- Document holds are frequently managed by in-house counsel.

  - If a document hold is narrowly distributed, be prepared to further distribute the hold as new custodians become known.

  - In-house counsel should monitor compliance with the hold for both electronic and hard copy documentation.

Whistleblowing for Lawyers Is Dangerous

1. Douglas v. DynMcDermott Petroleum Operations Co., 144 F.3d 364 (5th Cir. 1994):

In-house attorney complained to the DOE about discrimination at her client/employer. To further her case, she gave information to the DOE about other complaints of discrimination at the company.

Fifth Circuit held that there was no exception to the ethical rules that allowed her to disclose information regarding other wrongs without client consent, which she did not have.

Whistleblowing for Lawyers Is Dangerous

2. Pang v. International Document Services, 2015 WL 4724812 (Utah).

In-house attorney reported improper business practices “up the ladder” (as required by Rule 1.13(f)). Attorney was fired and brought suit for retaliatory discharge.

Utah Supreme Court held that the attorney was an employee at will, could be fired for any reason, and the ethical requirement that he report “up the ladder” was insufficient to overcome the general public policy in favor of employees being at will.

But See *Van Asdale v. International Game Technology*, 587 F.3d 989 (9th Cir. 2009), the Ninth Circuit reinstated a claim for wrongful discharge under Sarbanes Oxley brought by two terminated in-house counsel. Held that reporting stock fraud was a protected activity.

Yates Memo & Cooperation

- In late 2018, Rod Rosenstein softened the 2015 “Yates Memo.”
- Now, to be eligible for cooperation credit, corporations must work in good faith to identify individuals who were substantially involved in or responsible for wrong doings and disclose that information to the DOJ.
- Companies are expected to focus on identifying individuals who were “substantially involved in or responsible for the misconduct.”
- No longer an “all or nothing” approach to cooperation; In the Civil context, DOJ attorneys can offer some credit even if the company does not qualify for maximum credit.
- Similarly, the SEC has an enhanced focus on individuals and now engages in separate settlement talks with corporations and their employees.

MANAGEMENT IN THE CROSS-HAIRS

- April 29, 2016, Assistant Att'y General Leslie Caldwell:

It is in the company's interest to find out what happened, it is in the company's interest to find out who is responsible, and it is in the company's interest to tell the Government who is responsible…

Yates Memo Expanded Potential Conflicts

- Arguably, the Yates Memo creates a presumptive conflict between the Company and every employee-witness:
  - Company is incentivized to protect shareholder interests by inculpating individuals; and
  - Individual employees already incentivized (leniency, immunity and monetary awards) to inculpate "up the chain of command."

Implications of Yates Memo for Investigators

- **Ethical implications:** "Upjohn Warnings" may need to be expanded to ensure interviewees understand the risks presented by corporate interest in naming individuals;

- **Practical Implications:**

  Individuals may be less willing to cooperate;

  Separate, independent counsel may be required more often, adding significant time and expense to the investigation;

  Separate counsel may (1) not cooperate, impeding ability of company to gather all necessary facts, (2) unilaterally report additional or contradictory information to regulators, (3) encourage whistleblowing or private litigation (employment/qui tam claims).

Handling Requests for Separate Counsel

- Indemnification and Advancement Obligations:
  - Bylaws;
  - Employment Agreement;
  - California Labor Code § 2802 & Corporations Code § 317; Delaware Corporations Code § 145.
- Pool Counsel
- Employee still has a duty of cooperation with the company

Post Investigation Consideration

- Final Work Product?
  - Written Report
  - Summary Presentation Format
  - Oral Report
- Who maintains the file?
- M&A issues: Who owns the privilege during diligence? After the transaction is closed?

Part III

ADVANCEMENT, INDEMNIFICATION & INSURANCE

In The Cross Hairs

- April 29, 2016, Assistant Att'y General Leslie Caldwell:

It is in the company's interest to find out what happened, it is in the company's interest to find out who is responsible, and it is in the company's interest to tell the Government who is responsible…

Protecting Officers & Directors

- Indemnification – determined after conclusion of matter.
  - Some rights are mandatory under state law (e.g., upon a successful defense)
  - Some are prohibited (e.g., acts of bad faith)
  - Some are permissive: need to be addressed in bylaws or by contract
- Advancement – covers defense costs

ByLaws

- Do bylaws grant mandatory advancement and indemnification to the “fullest extent permitted by law”?
- Do the rights explicitly extend to *former* officers and directors?
- Does Delaware law apply? Forum?

Contractual

- Separate Agreements Should
  - Broadly Define “Fees” “Expenses” and “Proceedings”
  - Triggering Events: Threatened Legal Action or Formal Filing?
  - Choice of Counsel
  - Procedures and Timing of Payments, Fees-On-Fees
  - Access to Documents and Witnesses
  - Prevent Impairment of Rights Through Amendment of Bylaws
  - Require Minimum D&O coverage

D&O

- Insurance may cover when company is unwilling or unable to advance or indemnify under its bylaws
  - Judgments and settlements even where a company is prohibited from doing so by law
  - Informal investigations at inception
  - Bankruptcy

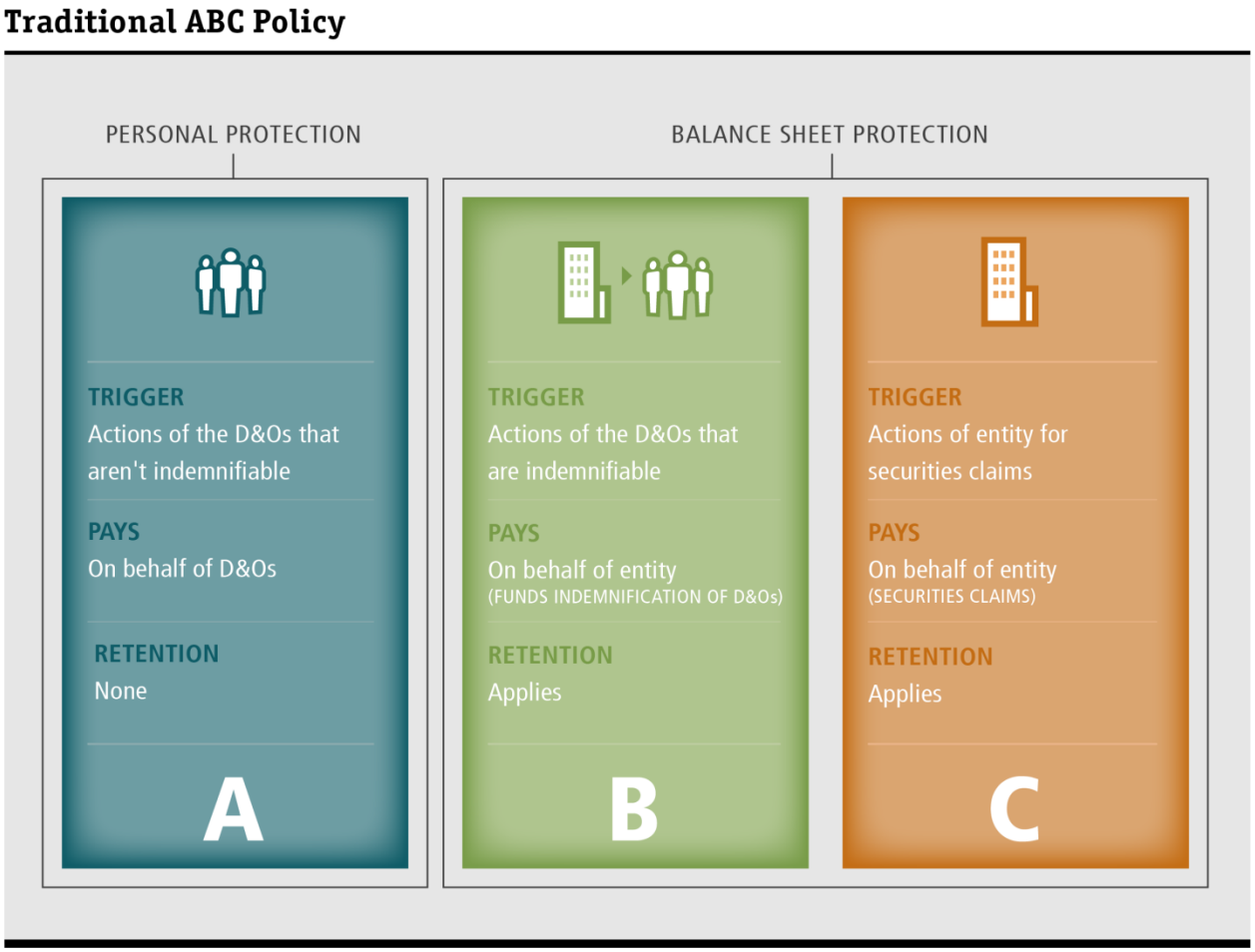
D&O Structural Coverage Overview - Traditional ABC Coverage

Traditional ABC policy strikes a balance between personal asset and corporate balance sheet protection

Side A: D&O Insurer pays when the Corporation cannot indemnify a Director or Officer (No Retention)

Side B: D&O Insurer reimburses the Corporation for its indemnification of the Directors and Officers (Retention applies)

Side C: D&O Insurer pays the Corporation for Securities Claims (In Securities suits, the Corporation is named in addition to directors and/or officers)

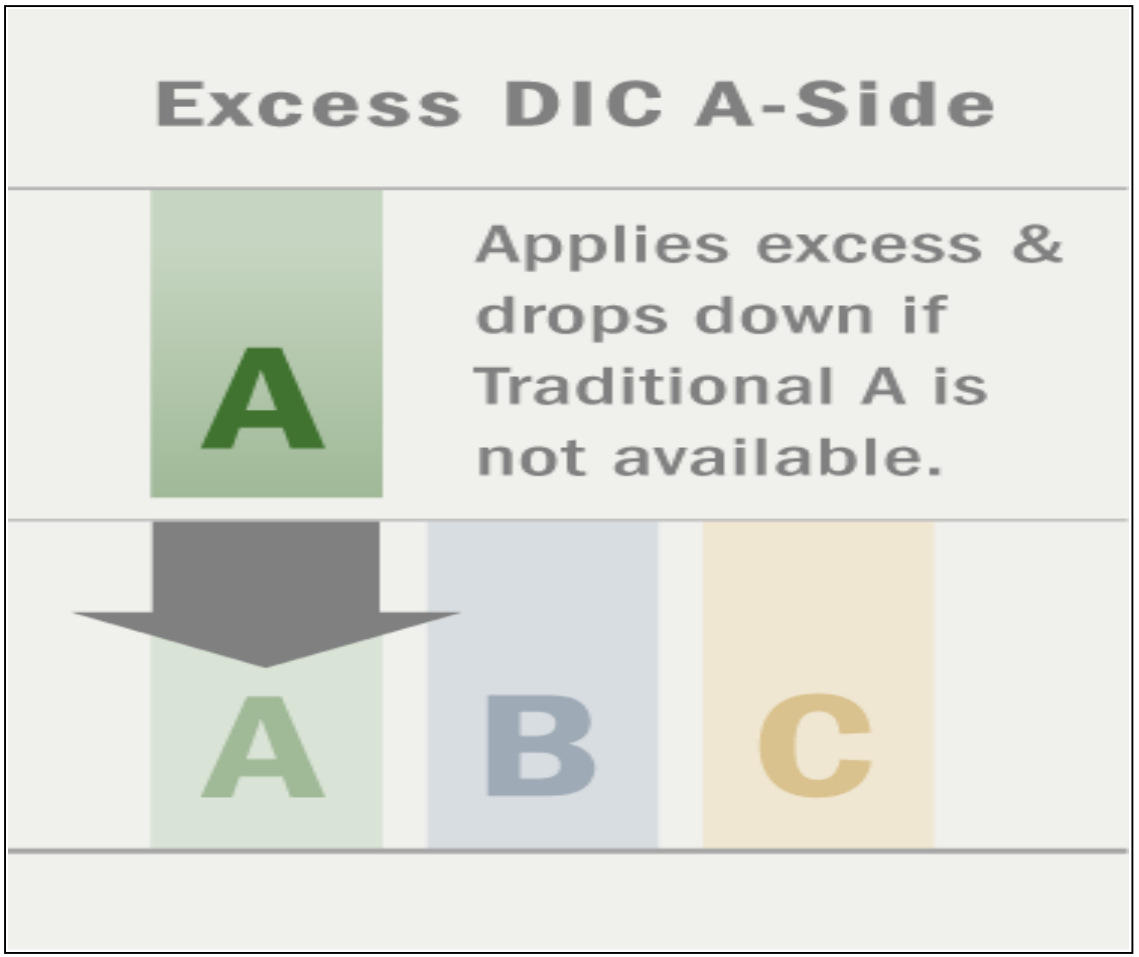


D&O Structural Coverage Overview - Side A DIC

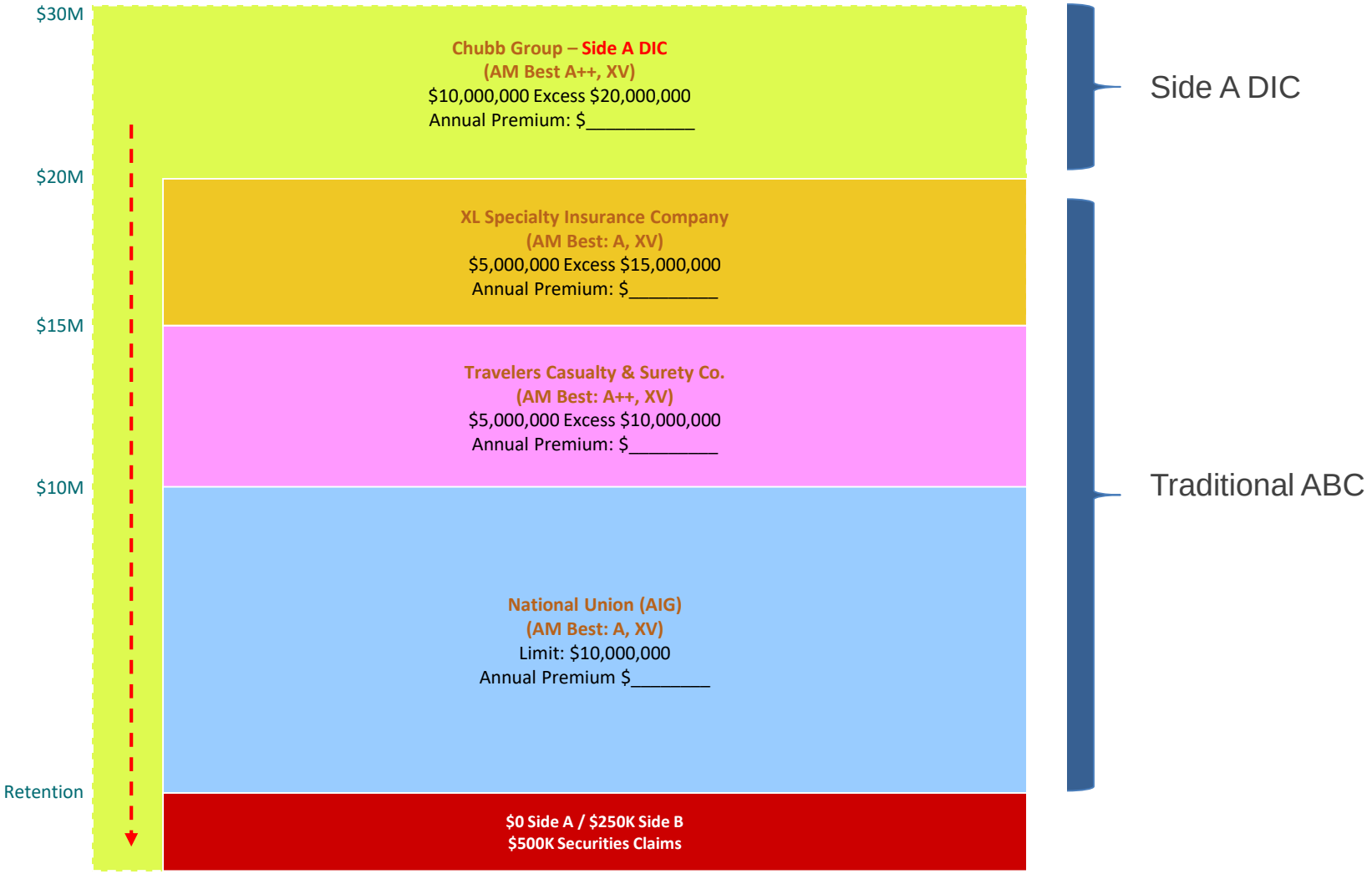
Side A DIC is a dedicated limit for the directors & officers – it is not "shared" with the Entity

Ensures maximum protection for Directors & Officers. If structured correctly, it will pay first-dollar when the Corporation cannot or will not defend or indemnify its directors and/or officer.

Also replaces an underlying insurer in the event the insurer becomes financially insolvent



Typical D&O Insurance Program Summary



Maximizing D&O

- **Problem: Single Limit**. Policy is shared among all three insuring agreements and among all insureds. Side C claim hits first and exhausts entire policy
- **Solutions:**
  - **Side A DIC Only.** Provides first-dollar coverage when the Company refuses to defend or indemnify Directors & Officers
  - **Priority of Payments.** Directors & Officers should be paid *before* the Corporation
  - **Advancement of Defense Costs.** Not just "reimbursement" at end of Claim

Maximizing D&O (contin.)

- Non-Rescindable Coverage for Side A
- Minimize All Exclusions. Exclusions for fraudulent or willful conduct should be narrow and defense costs should be paid up to final, non-appealable adjudication. In particular, remove: Insured vs. Insured Exclusion.
- Severability Provisions:
  - *Exclusions*. Include a provision stating that no conduct of any Insured Person will be imputed to any other Insured to determine the application of any exclusions for the purposes of determining coverage.
  - *Rescission*. Also include a severability provision specific to the issue of *application disclosures* which prevents the knowledge of, or material misrepresentation by, that bad actor from being imputed to the innocent insureds or the company as a whole.

Questions?

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