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CORPORATE MONITORS

Patterson Belknap attorneys Harry Sandick and Ryan Kurtz examine recently announced policy changes from the DOJ regarding the appointment of corporate monitors in criminal matters. The authors note that the changes appear to raise the internal hurdles that prosecutors must clear before seeking a monitor.

INSIGHT: DOJ Announces Changes in Corporate Monitorship Policy

BY HARRY SANDICK AND RYAN J. KURTZ

On Oct. 12, 2018, recently confirmed Assistant Attorney General Brian Benczkowski announced the issuance of a new policy memorandum entitled ''Selection of Monitors in Criminal Division Matters'' (the Benczkowski Memo). The Benczkowski Memo represents just the fourth known time the Department of Justice has addressed this subject in formal written guidance.

Benczkowski made this announcement at an event at NYU School of Law in which he explained that the purpose of the new policy memorandum was ''to further refine the factors that go into the determination of whether a monitor is needed, as well as [to] clarify and refine the monitor selection process.''

The release of the Benczkowski Memo is timely. In the years since the 2008 financial crisis, corporate criminal prosecutions have resulted in the imposition of corporate monitors with increasing frequency. In particular, over the past five years, the resolution of approximately one in three corporate prosecutions has included a monitorship condition. In some cases, corporate monitorships cost millions of dollars and involve day-to-day oversight.

In his prepared remarks, Benczkowski acknowledged the burdens of corporate monitorships, and the new DOJ memorandum appears to raise the internal hurdles that prosecutors must clear before seeking a monitorship condition when resolving the investigation or prosecution of a corporation.

The Scope of the Benczkowski Memo

The Benczkowski Memo applies to matters handled by the DOJ Criminal Division, not to matters handled by other components of the DOJ (such as the Antitrust Division or the Civil Rights Division).

It also applies when the DOJ is investigating or prosecuting a business organization (such as a corporation or partnership), and appears to have no relevance to the selection of monitors in other contexts (such as when a municipality or police department is being investigated).

Finally, it applies regardless of the type of disposition that the DOJ is proposing: a deferred prosecution agreement, a nonprosecution agreement, or a plea agreement.

Building on Prior Guidance

The Benczkowski Memo follows three prior DOJ statements on the subject of corporate monitorships.

In 2008, Acting Deputy Attorney General Craig Morford issued written guidance (the Morford Memo) on the subject of how a monitor should be selected. In 2009, Benczkowski's predecessor, former Assistant Attorney General Lanny Breuer, issued further guidance on this subject of monitorships (the Breuer Memo). A brief 2010 memorandum by former Acting Deputy Attorney General Gary G. Grindler added a requirement that monitorship agreements explain what role the DOJ might play in future disputes between a monitor and a corporation.

The Benczkowski Memo is the most extensive and thorough of the DOJ policy statements. By its terms, the Benczkowski Memo supersedes the 2009 Breuer Memo, but leaves in place the 2008 Morford Memo.

Weighing Costs, Benefits of a Monitor

The Benczkowski Memo continues longstanding policy by reminding prosecutors to weigh ''the potential benefits that employing a monitor may have for the corporation and the public'' against ''the cost of a monitor and its impact on the operations of a corporation.'' The costs are borne by the corporation's shareholders—who are ordinarily innocent bystanders to any criminal activity. This makes it important for the DOJ to conclude that the monitor is necessary to assure compliance in the future, and not merely useful.

The Benczkowski Memo expands on this prior guidance, providing federal prosecutors with a list of specific factors to consider.

On the ''potential benefits'' side of the equation, the memo directs prosecutors to weigh the following four considerations (quoted verbatim below):

- whether the underlying misconduct involved the manipulation of corporate books and records or the exploitation of an inadequate compliance program or internal control systems;
- whether the misconduct at issue was pervasive across the business organization or approved or facilitated by senior management;
- whether the corporation has made significant investments in, and improvements to, its corporate compliance program and internal control systems; and
- whether remedial improvements to the compliance program and internal controls have been tested to demonstrate that they would prevent or detect similar misconduct in the future.

In considering whether other remedial measures taken by the corporation to ensure future compliance are sufficient, prosecutors must consider ''the unique risks and compliance challenges the company faces, including the particular region(s) and industry in which the company operates and the nature of the company's clientele.''

If remedial measures short of a monitor are ''demonstrated to be effective and appropriately resourced at the time of the resolution'' of the matter, ''a monitor will likely not be necessary.'' In the event that prosecutors deem a monitorship necessary despite the burdens it imposes, the prosecutors must ensure that ''the proposed scope of a monitor's role is appropriately tailored to avoid unnecessary burdens to the business's operations.''

In sum, a monitorship is appropriate ''only where there is a demonstrated need for, and clear benefit derived from, a monitorship relative to the projected costs and burdens.'' Otherwise, the DOJ should use other means to enforce compliance.

Any monitorship term in an agreement with the Criminal Division should also include a number of specific provisions aimed at making sure that the monitor's work is bounded by subject matter and time frame.

In particular, the agreement should include the following six items:

- a description of the monitor's required qualifications;
- a description of the monitor selection process;
- a description of the process for replacing the monitor if necessary;
- a statement that monitor selection will be completed within 60 days;
- an explanation of the responsibilities of the monitor and the monitorship's scope; and
- the length of the monitorship.

Centralized Approval for Monitorships

The memo also increases the hurdles that a prosecutor must clear to secure internal approval to include a monitor as a condition of resolving an investigation or prosecution. The Morford Memo required prosecutors to, ''at a minimum, notify the appropriate United States Attorney or Department Component Head prior to the execution of an agreement that includes a corporate monitor.'' The Benczkowski Memo, by contrast, requires that prosecutors ''receive approval from their supervisors, including the Chief of the relevant Section, as well as the concurrence of the Assistant Attorney General . . . for the Criminal Division or his/her designee'' before agreeing to the imposition of a monitor.

Given the significance of the decision to appoint a monitor, and the need for national uniformity, it makes sense that centralized approval would be required.

A Fair Selection Process

In his remarks at NYU, Benczkowski expressed a desire to ensure public confidence in the monitor selection process, avoiding conflicts of interest and ''any suggestion that monitors are chosen for inappropriate reasons, including personal relationships or past employment at the Department.'' The Benczkowski Memo requires that the Office of the Deputy Attorney General approve all monitor candidates proposed by the corporation to-be-monitored following reviews by the prosecutors assigned to the case, a DOJ standing committee, and the Assistant Attorney General.

The in-depth, layered review process is designed to ''(i) instill public confidence in the process; and (ii) result in the selection of a highly qualified person or entity, free from any actual or potential conflict of interest or appearance of a potential or actual conflict of interest, and suitable for the assignment at hand.''

The Benczkowski Memo lays out the specifics of this process: Once it is decided that a monitor will be appointed, company counsel will be asked to submit a written proposal identifying three candidates, along with a description of each nominee's qualifications and a series of written certifications from the monitor and the company that are aimed at avoiding a conflict of interest. The Criminal Division attorneys handling the case must interview the candidates and prepare a recommendation to the Standing Committee.

The Standing Committee will consist of:

- the Deputy Assistant Attorney General who supervises the Fraud Section within the Criminal Division,
- the Chief of the Fraud Section (or whichever section is supervising the prosecution), and
- the Deputy Designated Agency Ethics Official for the Criminal Division.

The Benczkowski Memo sets out a detailed series of steps that the Standing Committee should take before the recommended candidate is reviewed, and approved or rejected, by the Assistant Attorney General for the Criminal Division, and by the Deputy Attorney General. Any deviation from the established procedure must be approved by the Standing Committee.

The Benczkowski Memo also reminds Criminal Division employees to provide written certification of compliance with the applicable conflict-of-interest guidelines.

Ramifications

Neither in the Benczkowski Memo, nor in the accompanying remarks made by Benczkowski, is there any express statement that the DOJ seeks to reduce the number of cases in which a monitor is imposed. At the same time, the changes appear to signal that prosecutors will be more selective about when to seek monitorships, and more mindful of the costs that monitorships impose. On balance, the Benczkowski Memo would seem to reduce the likelihood of the appointment of a monitor in a given case.

The specific factors enumerated in the Benczkowski Memo will be useful to defense counsel who are advocating against the appointment of a monitor. A corporation can reduce its risk of incurring a monitorship by terminating wrongdoers, implementing more robust internal controls, and conducting internal audits to demonstrate the effectiveness of new safeguards. In discussions with the DOJ, a corporation should be prepared to discuss in detail its revised internal compliance controls, while also explaining the potential cost of a monitorship.

Time, effort, and money spent on the development of a new, more effective compliance plan could tip the benefit/burden balance against appointing a monitor. Defense counsel should explain why the appointment of a monitor is disproportionate to the prior conduct and the risks going forward.

For example, a problem that only arose in a single business unit or geographic office might not require a monitor when the problems in that unit have been identified and remediated. In addition, the Benczkowski Memo directs prosecutors to consider whether a monitorship is appropriate ''at the time of the resolution'' of the prosecution. Inherent in this concept is a recognition that whatever compliance failures might have existed during the time of the criminal activity should not be held against the company if it has turned over a new leaf.

In Benczkowski's remarks that accompanied the announcement of the new policy, he also explained that the Criminal Division would be hiring a number of individuals with a specific compliance focus. These will be attorneys with ''experience developing and testing corporate compliance programs.'' This represents a slight shift from the use of a single compliance counsel, located in the Fraud Section, to review compliance issues throughout the Criminal Division. One would expect that these new compliance-minded attorneys will be able to help carry out the cost-benefit weighing contemplated by the Benczkowski Memo.

Practitioners should also bear in mind that prosecutors must now navigate several layers of DOJ hierarchy in order to secure approval to seek a monitorship, and several more afterwards to select a monitor. Prosecutors may be more amenable to compliance-ensuring conditions, short of monitorship, that do not involve such an extensive DOJ approval process. The various levels of review also provide opportunities for defense counsel to advocate against the appointment of a monitor.

Finally, by its terms, this new guidance does not impact the decision to select a monitor in the settling of alleged civil rights violations or police misconduct—those are outside the scope of the Benczkowski Memo. This guidance is limited to cases within the Criminal Division, and will primarily impact criminal prosecutions brought by U.S. Attorneys' Offices or by the Fraud Section within the Criminal Division at Main Justice.

Author Information

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