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A Guide to Corporate Internal Investigations – Part I

By Jennifer L. Chunias and Jennifer B. Luz*

In this two-part article, the authors set forth a framework of best practices and considerations for conducting effective internal investigations, as well as the most common pitfalls to avoid. This first part of the article discusses the threshold issue to consider when deciding whether to investigate, staffing the investigation, goals and parameters of the investigation, and document review. The second part of the article, which will appear in an upcoming issue of Pratt's Privacy & Cybersecurity Law Report*, will focus on witness interviews, a public relations strategy, and concluding the investigation.*

In-house teams at public and private companies are confronted almost daily with evidence or allegations of potential internal wrongdoing. These scenarios may vary widely in severity and magnitude—from notification of a government investigation into potential violations of federal law by a member of senior management, to a routine internal complaint of violations of the company code of conduct or employee policy. In most instances, the company would be best served by conducting some type of internal review into the allegations. However, deciding whether and how to conduct an internal investigation requires consideration of a variety of factors. These typically include the nature of the corporation, the specific conduct, subject matter, and alleged actor(s) at issue, the applicable law, and, where appropriate, the government's enforcement priorities. And if an internal investigation is undertaken, there are a number of decisions that should be made at the outset, including who should conduct the investigation, the goals and parameters of the review, and whether a report—written or oral—will be issued. This article sets forth a framework of best practices and considerations for conducting effective internal investigations, as well as the most common pitfalls to avoid.

DECIDING WHETHER TO INVESTIGATE

The threshold issue to be considered upon learning of potential wrongdoing is whether to initiate an internal investigation at all. On balance, most scenarios warrant *some* kind of internal investigation, both for business purposes and in the event of scrutiny by government regulators or potential private litigants. U.S. regulators increasingly expect that

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companies will monitor their own conduct and report potential wrongdoing to the appropriate enforcement agencies. Likewise, private plaintiffs are filing more cases with significant allegations that attempt to call corporations' conduct into question. Under the right circumstances, conducting an effective internal investigation protected by the attorney-client privilege can benefit the company in a number of ways:

- Developing a comprehensive understanding of the facts necessary to assess a company's potential criminal and civil exposure;
- Remedying the conduct to prevent further violations;
- Memorializing the company's good faith response to the facts as they become known;
- Insulating senior management and/or the company board against allegations of complicity; and
- Promoting a culture of transparency and compliance.

If it appears that the government has already initiated an investigation into the alleged conduct or that one is probable, then the case for initiating an internal investigation is even stronger. It is almost always in the best interests of the company to gather information to allow it to respond effectively to the government. By controlling the facts, counsel is best equipped to argue against prosecution and to respond to government requests. An internal investigation also reduces surprises that may arise during a government investigation, allowing the company's legal advisors to stay ahead of the outside investigators.

The incentive for a company to conduct an internal investigation in order to stay ahead of the government and gather the information necessary to respond effectively and promptly to government inquiries has only increased in recent years, in light of the so-called "Yates Memo." In September 2015, former Deputy Attorney General Sally Yates issued a memorandum to prosecutors within the Department of Justice regarding "Individual Accountability for Corporate Wrongdoing," commonly referred to as the "Yates Memo." The Yates Memo reflects the Department of Justice's increased focus on individual wrongdoing in the context of corporate investigations following the perceived shortcomings of enforcement actions during the financial crises that resulted in billions of dollars in penalties but no individual prosecutions. It therefore requires that a company under investigation "provide to the Department all relevant facts about the individuals involved in corporate misconduct" in order to qualify for any cooperation credit.[1] Under the Yates Memo, a company is encouraged

[1] To some commentators, the Yates Memo signaled a potentially dramatic shift in the Department of Justice's approach to investigating and prosecuting corporate wrongdoing. In reality, the Yates Memo largely streamlined and emphasized long-standing Department of Justice guidance directing prosecutors to investigate individual wrongdoing as zealously and diligently as corporate wrongdoing, and to bring civil or criminal charges against individual defendants where warranted. A significant increase in the prosecutions of individual defendants in the wake of the Yates Memo is not yet apparent.

to "do investigations that are timely, appropriately thorough and independent, and report to the government all relevant facts about all individuals involved, no matter where they fall in the corporate hierarchy."

Depending on the nature of conduct at issue, the Yates Memo raises the stakes for a company deciding whether to conduct an internal investigation when faced with allegations of wrongdoing. As Ms. Yates said at the time: "If they [companies] want any cooperation credit, they will need to investigate and identify the responsible parties, then provide all non-privileged evidence implicating those individuals."[2] By "cooperation credit," Ms. Yates was referring to the U.S. Federal Sentencing Guidelines (the "Guidelines") for corporations, which affect a corporation's civil or criminal penalty and is determined not just by the underlying crime, but by the conduct of a corporation before and during any government investigation.

For example, the Guidelines provide for an increase in criminal fines to be imposed on corporations in connection with criminal violations of federal law if senior corporate personnel "participated in, condoned, or [were] willfully ignorant of the offense" or if "tolerance of the offense by substantial authority personnel was pervasive throughout the corporation."[3] On the other hand, the Guidelines provide for a reduction in a corporate criminal fine under certain circumstances, such as if the criminal offense occrred despite "an effective program to prevent and detect violations of law."[4] There is a presumption that the program was not effective if senior management participated in, condoned, or were willfully ignorant of the offensive conduct.[5]

If, however, upon learning of potential misconduct, a company promptly undertook an internal investigation and implemented appropriate remedial action, this can assist a company in arguing against the imposition of criminal or civil penalties. Previously, a company could receive partial credit for "significant" cooperation in an investigation. However, the Yates Memo made clear that a company must provide the Department of Justice with facts regarding individual wrongdoing as a threshold requirement in order to be considered for cooperation credit. As such, under this policy, the incentives for a company to

[2] Yates, Sally. "Deputy Attorney General Sally Quillian Yates Delivers Remarks at New York University School of Law Announcing New Policy on Individual Liability in Matters of Corporate Wrongdoing," Thursday, September 10, 2015, *available at* https://www.justice.gov/opa/speech/deputy-attorney-general-sally-quillian-yates-deliversremarks-new-york-university-school.

[3] U.S.S.G. § 8C2.5(b)(1)(A)(i)-(ii).

[4] § 8C2.5(f)(1).

[5] § 8C2.5(f)(3)(B).

conduct a thorough, independent, and properly scoped and documented investigation at the outset are more compelling than ever.[6]

The results of an internal investigation also can help the company determine how to proceed in its discussions with the government during a government investigation. Among other things, it will help a company decide whether it should seek to settle the government investigation or persuade the government to agree to a favorable settlement. In the event that a government investigation is threatened but has not yet been initiated, disclosing the results of an internal investigation may assist the company in persuading the government that no government investigation is necessary, or that the government investigation need not be as far-reaching as it might otherwise be.

A careful internal investigation also allows the corporation to discuss the subject matter of the investigation with employees and potentially mitigate unnecessarily harmful testimony down the road. It may provide an opportunity to help lock in the testimony of witnesses at an early stage. An internal investigation is also particularly prudent if private litigation has been commenced or is probable. A prompt and effective internal investigation and appropriate remediation of certain allegations of misconduct may assist a company in mounting a successful affirmative defense in private litigation. Finally, an internal investigation allows a company to assess its systems and controls, and to develop an apropriate system of remedial measures to address any deficiencies.

Whether to initiate an internal investigation may be a more difficult decision when the government has not yet initiated an investigation or is unlikely to do so. Despite its many benefits, an internal investigation does have certain costs. They generally do not override the need for an internal investigation, but the potential costs of such a review must nevertheless be addressed. For instance, if the investigation is not privileged, it

[6] Since the Yates Memo was issued 19 months ago, there are signs that the Department of Justice is placing pressure on companies to help hold executives accountable. For instance, on June 3, 2016 the Criminal Division of the Department of Justice closed its investigation of Nortek, Inc. for possible violations of the Foreign Corrupt Practices Act ("FCPA") due to, among other factors, Nortek's "full cooperation in this matter (including by identifying all individuals involved in or responsible for the misconduct and by providing all facts relating to that misconduct," Nortek's "agreement to continue to cooperate in any ongoing investigations of individuals," and Nortek's remediation which "include[ed] terminating the employment of all five individuals involved in the [FCPA] misconduct, which included two high-level executives of the China subsidiary." Letter from Daniel Kahn, Deputy Chief of Fraud Division at the Department of Justice, dated June 3, 2016, *available at* https://www.justice.gov/criminalfraud/pilot-program/declinations. On the civil side, in September 2016 the Department of Justice included two senior executives of North American Health Care Inc., its chairman of the board and its senior vice president, in a civil settlement agreement for potential False Claims Act violations, in which the executives agreed to pay $1.5 million out of the $28.5 million settlement. *See* https://www.justice.gov/opa/pr/north-american-health-care-inc-pay-285-million-settleclaims-medically-unnecessary. It is still an open question whether the new administration will continue to prioritize the policies of the Yates Memo as vigorously as the prior administration, but comments from Attorney General Sessions and President Trump indicate that there is unlikely to be any sea change in this area for the time being.

could create a roadmap for government officials and private (perhaps class action) litigants. Even if counsel has faithfully cloaked an investigation with layers of privilege, the company may be forced (or, at least, strongly encouraged) to waive that privilege and share all aspects of its internal investigation with the government. Finally, an internal investigation can be disruptive and costly in terms of fees and lost business opportunities. Document collection, e-mail review, and difficult questions in interviews may be distracting and impact employee morale. Ideally, the internal review remains privileged and confidential from the public, but there also could be reputational concerns if the investigation becomes known to the public.

But despite the potential costs, it is almost always preferable to get to the bottom of the matter. For one thing, a company's willingness and capacity to conduct an effective internal investigation is an important component of an effective compliance program. And senior management has an obligation to take appropriate steps when confronted with indications of potential misconduct. Conducting an internal review *now* also can avoid exposing the company and board to risk of regulatory action or private litigation later—if, for instance, the problem goes undetected or is not remediated and, ultimately, recurs.

STAFFING THE INVESTIGATION

Despite the potential costs, in most instances an internal investigation is necessary. The next decision is who should conduct the investigation. Generally speaking, the answer to this question depends on the nature and seriousness of the allegations, as well as the strength of the evidence suggesting misconduct has occurred.

Counsel, Auditors, or Human Resources

Allowing internal auditors, compliance personnel, or human resources staff to conduct the investigation (as opposed to in-house or outside counsel) may be less disruptive and could decrease the employees' level of concern over the seriousness of the situation. Such internal reviewers may also be the most economical solution. In-house or retained counsel, however, may b more experienced or better skilled at conducting an investigation. Counsel may also have greater objectivity and independence in assessing the progress and results of the investigation. Further, attorneys are often asked to provide legal services based on the results of the investigation. For instance, it is possible that there will be the need for company counsel to deal with law enforcement or regulatory agencies in connection with the subject matter under review, and it may be most advantageous for these attorneys to be intimately familiar with the facts and results of the internal investigation. Most important, counsel will cloak the investigation with the attorney-client and work product privilege.

In-House Counsel or Outside Counsel

If counsel is selected to lead the internal investigation, the next question is whether the company should use in-house or outside counsel. The following general factors should be considered in determining whether the investigation is sufficiently serious to warrant the retention of outside counsel: the seniority and prominence of the individuals who will likely be the subject of the investigation; the potential financial exposure to the company; and the extent to which the subject matter of the review is likely to result in law enforcement activity.

Outside counsel present a number of benefits. For instance, in most cases, outside counsel will be more objective and, perhaps more important, will *appear* more objective to outsiders, including the government. Such independence may be important to prosecutors who may seek to rely on reports or presentations provided by counsel conducting the investigation. If the subject matter of the investigation implicates senior management or the legal department, the independence of the outside law firm might provide the board of directors additional comfort in relying on the results of the investigation.

Outside counsel also frequently have greater resources and more experience in conducting internal investigations.

In-house corporate counsel are busy running a business or managing disparate litigations. Outside counsel, on the other hand, are in the business of conducting investigations.

Outside counsel also may provide a greater degree of privilege protection. While the attorney-client privilege and attorney work product doctrine can apply to the work of in-house attorneys, courts have applied stricter standards to in-house counsel in determining whether material is protected. The work of in-house counsel is more likely to be viewed as "business" in nature, whereas courts are less likely to find that a business purpose was the primary purpose of an internal investigation if that investigation is conducted by outside counsel.

On the other hand, in-house counsel have a greater familiarity with their own organization and will not have to spend time learning the industry. And the presence of outside counsel may increase the level of concern among employees. Depending on the circumstances, it may make the most sense to implement a staged approach, with in-house counsel handling the investigation during its early stages, consulting with outside counsel as needed, and ultimately turning the investigation over if it escalates. For one thing, the expense of outside counsel cannot be undertaken every time a company needs to conduct an inquiry into potential wrongdoing. In addition, especially at the early stages, it may make the most sense to leverage in-house counsel's superior knowledge of the company's business, procedures, and personnel.

In the event the decision is made that outside counsel should lead the investigation, additional consideration should be given to whether the company's existing outside counsel or an unaffiliated law firm should conduct the investigation. This decision turns in large part on the need for a truly "independent" review. For instance, if the allegations involve the board as a whole, it may make the most sense to form a committee of new directors or independent directors, who should retain an unaffiliated law firm to assist. If the allegations implicate high-level executive officers, the investigation most likely should be overseen by the Audit Committee or other independent directors, which typically will choose an unaffiliated law firm to assist. If the allegations involved non-executive managers or other employees, in-house counsel or other regular outside counsel generally should oversee the investigation.

Other Outside Consultants or Forensic Investigators

Internal investigations often require the assistance of private investigators, forensic accountants, technology experts, and other specialized consultants who can be helpful in fact-finding and analysis of data. One of the decisions that must be made early in an investigation is whether to rely on in-house expertise or outside experts for that expertise. Although personnel who are already familiar with the matters at issue may be most efficient in many cases, this may put these personnel at risk of having to testify regarding the factual analysis performed in connection with the investigation.[7]

Steps also must be taken when using non-attorney consultants or investigators to protect the privileged nature of the work. Among other things, counsel, preferably outside counsel, should retain the consultant. Retainer letters should state that the consultant is retained by counsel in anticipation of litigation, subjecting all consulting work to the attorney-client privilege and work product doctrine. Reports, if any, should be created only upon request of counsel, and, if created, such reports should state at the outset that they were created at the direction of counsel. All documents should be addressed and sent to counsel with the usual and appropriate "Privileged and Confidential; Attorney Work Product" label.

Cross-Border Issues

The company should pay special consideration to issues that may arise if the internal investigation involves operations, subsidiaries or employees located in another country, and plan accordingly at the outset. Such cross-border investigations are becoming increasingly common and can raise thorny issues for an investigation. The laws of the foreign jurisdiction may impact how the investigation proceeds. For example, the company should be aware of data privacy concerns when gathering data and documents for review. Countries as varied as Germany, Turkey, and Russia have data privacy laws that are more protective over employee emails and personal data than the laws in the U.S. These laws can impact the ability to collect, the ability to review,

[7] *See, e.g., In re Six Grand Jury Witnesses*, 979 F.2d 939 (2d Cir. 1992).

the location where review can occur, and how the data can be stored. For example, in many countries, written employee consent is required to access employee company email accounts and personnel data.

In addition, depending on the laws of a particular jurisdicton, there may be mandatory disclosure requirements if the investigation uncovers evidence of particular misconduct or a crime in that jurisdiction. Issues may also arise if the company chooses to discipline or terminate employees in a foreign country. Decisions such as those involving severance to a discharged employee or concerns about discrimination can implicate local employment laws.

In order to prepare for and respond to these types of issues, the company should consider engaging local counsel and local forensic resources to assist with the internal review. While U.S. companies will likely want to retain an experienced, U.S. based law firm to oversee the investigation to ensure compliance with U.S. law, the U.S. firm may not have any expertise in the laws of the relevant jurisdiction. As such, depending on the nature of the allegations at issue, it may be prudent to engage a qualified local counsel at the outset of the investigation. That way, the investigative team in the U.S. will know in advance what issues may arise during the investigation and what legal factors must be considered. Local counsel can also be on hand to assist with witness interviews, potential employment actions or other remedial measures. Local counsel advice can provide a company with comfort that it is making an informed decision based on the interests of the client and the likely legal consequences with the assistance of experienced local counsel.

GOALS AND PARAMETERS OF THE INVESTIGATION

Once decisions are made to investigate and regarding who will handle the investigation, the company must set the goals and parameters of its work. A typical internal investigation can accomplish a number of goals, including:

- developing the facts and evidence;
- determining the extent of potential civil and criminal liability;
- formulating a strategy for future compliance; and
- remedying past misconduct.

Once the goals are established, the team should determine the appropriate scope of the review. Internal investigations of every size require balancing efficiency with quality, thoroughness, and completeness, and one of the biggest challenges to any investigation is designing the scope of the review so that it is sufficiently thorough, while not overly broad. This effort can have critical implications on the credibility of the investigation, as well as the costs.

Approaching an investigation in phases and staying focused on specific issues or allegations can help manage costs and avoid "mission creep." Likewise, it is generally

sensible to start with a set of preliminary investigative steps to identify supporting evidence that would help the company determine the need to probe further. While a broad investigation will likely produce more information and will put the company in a better position to assess its overall exposure, the more detailed the investigation, the greater the internal disruption and the more likely the investigation will open the proverbial "Pandora's box." When the U.S. government is involved, companies also must make sure they reach an agreement with authorities on a reasonable strategy.

A related point to consider at the outset is the timing of the investigation. Depending on the nature of the investigation, this could be dictated by outside factors, most notably, the government. The length of the investigation is, of course, also contingent on its scope: how much information needs to be gathered and reviewed. But an extended investigation risks information leaks and further disrupts business.

To ensure the effectiveness of the investigation, a control group should be established and be involved in developing a strategy for the investigation. Among other things, this group will determine who needs to be informed about the investigation. Although confidentiality must be considered and carefully preserved, certain supervisors and managers will need to know what is happening in order to facilitate the collection of documents and the scheduling of employee interviews.

Clear direction also must be provided to employees and managers as to the confidentiality of the investigation. Employees should be instructed as to how they should respond to inquiries from the government, media, or other outside parties. Cooperation of employees should be expected and received, but employees, of course, have competing concerns: if an employee is a subject or target of a criminal investigation, the employee may choose to invoke the Fifth Amendment and refuse to cooperate, regardless of the employment ramifications.

The investigative team should identify key documents, employees, and other information to be evaluated during the investigation at the outset. Finally, the team should consider how the results of the investigation will ultimately be reported. Beginning with the end in mind will save time and help the investigation stay more organized as it moves ahead.

DOCUMENT REVIEW

Document review is a critical component of any internal investigation. Among other things, documents can assist counsel in obtaining information from witnesses, and in educating law enforcement officials on the issues under review. That being said, the most expensive aspect of an internal investigation is usually the review of documents and associated technology costs. While this is often an unavoidable reality of an investigation, care should be taken by the investigative team to scope document review reasonably, and not overly broad unless the initial findings warrant a deeper dive.

As soon as the company becomes aware of allegations or evidence of misconduct, it should suspend normal document retention procedures and preserve all relevant documents relevant to the subject matter of the investigation, including e-mails. If the company has become a target or subject of an investigation, potentially responsive documents cannot be destroyed, regardless of general document retention policies. A diligent search should be conducted to locate and secure documents that relate to the subject transaction or incident.

It is important to review and become familiar with all documents potentially relevant to the investigation, even those that are not responsive to any pending document requests or subpoenas, including:

- Policies, procedures, and manuals;
- All emails and other electronic data, including, if economically feasible, archived emails;
- Personnel files;
- Minutes from Board of Directors meetings and related Board materials; and
- Privileged documents that are not subject to production.

If the government has opened its own investigation, it may request that the company produce documents on certain topics. A thorough document review gives investigators a preliminary understanding of the factual landscape so that it may position the company in the best light while remaining forthcoming to the government. It also provides context for the next step of the investigation—witnss interviews—and helps the investigators develop the facts and questions for each interview.

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The second part of this article, which will appear in an upcoming issue of *Pratt's Privacy & Cybersecurity Law Report,* covers witness interviews, a public relations strategy, and concluding the investigation.