Anti-Corruption Report
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June 12, 2019

INTERNAL INVESTIGATIONS

Conducting Internal Investigations in the Shadow of *U.S. v. Connolly*

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In her recent decision in *United States v. Connolly*, Chief Judge McMahon of the U.S. District Court for the Southern District of New York sharply criticized the Department of Justice for "outsourc[ing] its investigation" of LIBOR manipulation to Deutsche Bank and its outside counsel.[1] Judicial oversight of internal investigations is uncommon because, even when companies disclose their findings to the government, they overwhelmingly enter into pre-indictment settlements to avoid enforcement actions.

Individual employees who are ensnared in these investigations, by contrast, have stronger incentives to test the government's case and challenge the charges against them. Such challenges and the decisions that have arisen from them have allowed courts to weigh in on government practices that generally go unquestioned. One of the most notorious examples of this was in *United States v. Stein*, the criminal tax case in the Southern District of New York, in which charges against 13 former KPMG employees were dismissed on the basis that the government improperly influenced KPMG to withhold attorney's fees and in turn interfered with their right to counsel. The landmark decision resulted in significant reforms, including the issuance of new DOJ guidance prohibiting the government from considering whether a company paid its employees' legal fees in assessing cooperation credit.

While it is still too early to predict whether the *Connolly* decision will have a similarly profound impact on how the government will conduct corporate investigations in the future, the decision does provide a rare glimpse into how companies balance their fiduciary obligation to conduct their own internal investigations with their sensible desire to cooperate fully with government authorities and their investigations.

The *Connolly* court was highly critical of the government's "outsourcing" of the investigative function to company counsel, but whether and to what extent that level of close coordination happens in the future will be a decision left to the government. The opinion also provides an opportunity for corporate counsel to reflect on how to conduct internal investigations in the shadow of the government and ensure that the interests of company shareholders and employees are being served without jeopardizing potential cooperation credit as part of future settlements.

See "Updates to the Corporate Enforcement Policy Attempt to Address Company Concerns" (Apr. 3, 2019).

United States v. Connolly

The *Connolly* case arose out of the LIBOR rigging investigation of several banks, including Deutsche Bank, by the Department of Justice and other federal agencies. Defendants Matthew Connolly and Gavin Campbell Black were indicted in connection with this investigation and were ultimately convicted by a jury of various crimes, including wire fraud. In the years leading up to the indictment, Deutsche Bank had conducted a sweeping internal investigation, and had ultimately entered into a deferred prosecution agreement with DOJ.

Black moved for relief – including dismissal of the indictment against him – under the Supreme Court's decision in *United States v. Kastigar*, which held that "[a]ny use, direct or indirect, of a defendant's compelled statements is unconstitutional under the Fifth Amendment's self-incrimination clause[.][2]"

Chief Judge McMahon found that Deutsche Bank's counsel had taken direction from the government on, among other things, whom to interview, when to interview them and how to interview them, and also provided the government with interview summaries and held weekly update calls for the final 14 months of the investigation and concluded that Deutsche Bank's internal investigation was "fairly attributable" to the government. Ultimately, however, the court held that the government did not violate *Kastigar* because it did not use Black's statements at trial, before the grand jury or during its investigation.

See "The ACR Brief: The DOJ Wants to Stay Out of Your Investigations" (May 22, 2019).

An Opportunity for Reform or Business as Usual?

Companies routinely cooperate when they are being investigated by the government, and DOJ encourages and incentivizes such cooperation. Cooperating with DOJ entails not only responding to document requests, but also furnishing facts gathered through interviews conducted by attorneys in the course of internal investigations, and sharing facts gleaned through witness statements or interviews conducted by non-attorney personnel. Judge McMahon said nothing to the contrary, but rather took exception to the level of cooperation between the government and Deutsche Bank's outside counsel, commenting that:

> rather than conduct its own investigation, the Government outsourced the important developmental stage of its investigation to Deutsche Bank—the original target of that investigation—and then built its own 'investigation' into specific employees . . . on a very firm foundation constructed for it by the Bank and its lawyers. This was no ordinary 'outside' investigation. Deutsche Bank did not respond to the Government's subpoenas by turning over documents without comment, and its employees were not subjected to government or regulatory depositions on notice, at which they were defended by company counsel. Indeed, Deutsche Bank did the opposite—it effectively deposed their employees by company counsel and then turned over the resulting questions and answers to the investigating agencies.

Of course, there is nothing inherently wrong with coordination between a company and the government in the course of parallel internal and government investigations. From the perspective of the company, cooperation can expedite investigations and secure favorable outcomes, and from the perspective of the government, cooperation can enhance the fact-finding ability of its investigators and save significant government resources.

Indeed, for all the critiques, Judge McMahon recognized that the investigation was a "conspicuous success for Deutsche Bank," and likely "save[d] the Government considerable time and precious resources[.]" And while the court was highly critical of the government's "outsourcing" of its investigation to counsel for Deutsche Bank, at no point did the court criticize the bank or its counsel – both of whom appear to have appropriately balanced the interests of the company to conduct a thorough investigation while undertaking investigative steps to obtain significant cooperation credit. In fact, Judge McMahon described Deutsche Bank's "conspicuous success," noting that the company entered into a DPA with the DOJ and "agreed to (*i*) pay $775 million in criminal penalties; (*ii*) continue cooperating with the Government in its ongoing investigation; and (*iii*) retain a corporate monitor for the three-year term of the agreement."

Did the government ask more of Deutsche Bank than it does in a typical corporate investigation? Perhaps. The Justice Manual, which provides guidance to DOJ prosecutors, notes that "[o]ften, the corporation gathers facts through an internal investigation. Exactly how and by whom the facts are gathered is for the corporation to decide." Indeed, when asked about the *Connolly* decision at ACI's May FCPA conference held in New York, Dan Kahn, Chief of the DOJ's FCPA Unit, noted that the DOJ's policy is not to tell companies what to do in an investigation. To the extent that his views reflect a broader sense of how the DOJ conducts its investigations, it seems at least plausible that – at least on facts found by Chief Judge McMahon – the government went further than usual here.

Distinct From *Stein*

Ultimately, however, it is for the government to decide whether such close coordination between prosecutors and corporate counsel is desirable or not. Notably, at no point in her opinion does Chief Judge McMahon say that such coordination is improper or that it should be curbed. Nor is there any reason that the government should not rely heavily on cooperating companies in white-collar cases – much like the government relies heavily on cooperating individuals in blue-collar ones. In this way, the *Connolly* decision differs from *United States v. Stein*, the 2006 decision that resulted in significant reforms in how the government acts in corporate investigations.

In *Stein*, KPMG was the target of a government investigation and initially agreed to pay for legal representation for employees who faced potential criminal liability in connection with the investigation. The government made clear, however, that it would not look favorably on this practice when deciding whether to indict KPMG. As a result, KPMG determined that it would pay legal fees only for employees who agreed to fully cooperate with the government, and who agreed not to exercise their Fifth Amendment right to remain silent. This policy ultimately resulted in multiple employees being denied legal fees for failing to cooperate with the government.

Jeffrey Stein, a senior KPMG partner, along with other KPMG employees, was indicted.[3] Judge Kaplan held that the government had violated the Fifth and Sixth Amendment rights of Stein and his co-defendants by causing KPMG to cut off payment of legal fees and defense costs.

At the time of the KPMG investigation, DOJ was relying on the Thompson Memorandum, which required prosecutors to consider certain factors when deciding whether to indict a corporate entity, including whether a company elected to pay the legal fees of its employees and whether a company continued to employ or support employees who asserted their Fifth Amendment privilege or otherwise refused to cooperate in government investigations. After Stein, DOJ superseded the Thompson Memorandum with the McNulty Memorandum, which prohibited prosecutors from considering whether a corporation paid its employees' legal fees, with an exception only where "the totality of the circumstances show that [such indemnification] was intended to impede a criminal investigation[.]"

Connolly is a fundamentally different case than *Stein* because, unlike inducing companies to withhold legal fees and defense costs from non-cooperating employees, there is nothing inherently wrong with coordinating closely with corporate counsel during the course of an investigation. Close coordination, however, presents some risks for the government, including that certain witness statements may not be useable, and in the most extreme instances, that cases could be dismissed if they are derivatively based on "compelled" statements. In the event that *Kastigar* violations in future cases result in statements being rendered unusable, or cases being dismissed, DOJ is likely to reconsider how it interacts with corporate counsel.

Protecting the Company's Best Interests While Cooperating

While the government will have to consider whether the *Connolly* decision should change how prosecutors interact with companies in the course of investigations, corporate counsel should reflect on what steps they must take to ensure they are satisfying both their fiduciary and ethical obligations. While cooperating with the government can help companies attain favorable results, including non-indictment and favorable settlements, companies and their counsel should be cognizant of competing fiduciary duties, contractual duties owed to employees and professional ethical rules.

Cooperating with the government and conducting parallel internal investigations may implicate various fiduciary duties. For example, internal and government investigations often benefit from the cooperation of board members and company officers. In some instances, those individuals may be reluctant to submit to interviews or otherwise cooperate with investigations. However, because cooperating with the government, including by complying with interview requests, is often in the best interest of a company, refusing to cooperate may be inconsistent with fiduciary duties of care and loyalty that those employees owe to their companies.

In addition, to the extent companies are closely cooperating with the government, they may have ethical obligations to provide enhanced warnings to employees beyond the standard *Upjohn* warning. Typically, counsel conducting internal investigations advise employees that they represent the company, and not the

employee, and that while the interview is covered by the attorney-client privilege, the company may waive that privilege. Where the company has already waived privilege, as it appears Deutsche Bank did in *Connolly*, it may be inadequate, and inaccurate, to say that the company *may* choose to waive the attorney-client privilege, instead of saying that the company has chosen to waive the privilege.

Relatedly, and depending on the jurisdiction in which they practice, counsel may have certain ethical obligations to advise employees of potential conflicts and of the possibility of retaining separate counsel. For example, Comment 2A to Rule 1.13 of the New York Rules of Professional Conduct provides that "the lawyer should advise any constituent whose interest differs from that of the organization . . . that the constituent may wish to obtain independent representation." In situations where company counsel interview an employee knowing that counsel will pass along those statements to prosecutors, and that those statements may then be used to develop a case against the employees, professional ethics likely require that counsel advise the employees that their interest does differ from that of the organization. Of course, counsel will have to walk a fine line as to what they can or cannot advise the employees, lest they reveal confidences about the government's investigation.

See "Crafting and Delivering Effective *Upjohn* Warnings" (Apr. 18, 2018).

Risks of Interfering With Ongoing Government Investigations

While the focus of the *Connolly* opinion was on what the court perceived to be excessively close coordination between the government and the bank, there are also concerns raised when corporate counsel takes steps that have not been sanctioned by the government. Judge McMahon noted in her opinion that "Deutsche Bank's counsel sought the Government's 'permission' to interview Gavin Black, who still worked at the Bank, for a fourth time—which is to say, Deutsche Bank *asked the Government for 'permission' to interview its own employee*."(emphasis in original).

Seeking permission to conduct such interviews, or at a minimum advising the government that such interviews will take place, is not uncommon and is furthermore prudent. The government may have concerns when corporate counsel conducts interviews of company employees without first providing the government with notice. The government may wish to keep its own investigation confidential and be concerned with "tipping off" an employee who might also be a subject of the investigation.

Alternatively, the government may wish to have the "first shot" at the employee, so that the employee does not receive a preview from corporate counsel of the sorts of questions he or she may be asked, and benefit from that rehearsal. In order to avoid having companies interfere with its investigation, the government may request "de-confliction," that is, that the company refrain from interviewing its employees before the government does. While

an obligation to comply with that request only arises after the request has been made, companies may be rightfully concerned about jeopardizing cooperation credit if they take steps, even unwittingly, to hinder the government's investigation.

See "Deciphering De-Conflictions: An Interview With WilmerHale's Kimberly Parker" (May 16, 2018).

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[1] No. 16 Cr. 0370 (CM) (ECF No. 432) (Opinion Denying Defendant Gavin Black's Motion for *Kastigar* Relief) (*Connolly*) (S.D.N.Y. May 2, 2019).

[2] *Id.* at 29 (citing *United States v. Kastigar*, 406 U.S. 441, 453 (1972)).

[3] 435 F. Supp. 2d 330, 361 (S.D.N.Y. 2006), *aff'd*, 541 F.3d 130 (2d Cir. 2008).