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DOJ Revises Its Principles for Prosecuting Corporations – Again

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The Department of Justice ("DOJ") has once again scaled back the tactics it employs investigating and prosecuting corporations. The policy changes announced last week by DOJ are the latest in the department's steady retreat from using waiver of the attorney-client privilege and work product protection as evidence of a company's cooperation with the government.

Beginning with the Thompson Memorandum in 2003,* DOJ revised its *Principles of Federal Prosecution of Business Organizations* to define the factors investigators are to consider when determining whether to charge a corporation with wrongdoing. Many of the factors bear upon the level of "cooperation" shown by a corporation during the investigation, including (1) the corporation's willingness to waive the attorney-client privilege and work product protections, (2) the corporation's willingness to give virtually unfettered access to company employees and other witnesses, and (3) the corporation's willingness to limit the amount of legal and financial aid it offers its employees, directors, and officers during the course of such investigation.

Partly as a result of criticism of these policies, DOJ revised the guidelines again on Dec. 13, 2006. Authored by U.S. Deputy Attorney General Paul McNulty, and known as the McNulty Memorandum, this revised policy limited the waiver requests to "rare circumstances." In addition, investigators were to obtain approval from higher levels within DOJ before seeking limitations on attorneys' fees expenditures, and waivers of attorney-client privileged communications and work product. Finally, prosecutors needed to demonstrate a legitimate need for such confidential, protected corporate information.

The McNulty Memorandum, however, did not ease DOJ's level of aggressiveness, nor did it quell intense criticism from the private legal community. Accordingly, on Aug. 28, 2008, DOJ again revised its guidelines, this time through a memorandum issued by Deputy United States Attorney Mark Filip (which will surely become know as the "Filip Memorandum"). The revised guidelines forbid federal prosecutors from pressuring corporations and their employees to waive certain protections during federal investigations. Although these pressures are no longer "demanded," DOJ still has its list of factors to consider.

Courts are also beginning to push back against demands by the government for privilege and work product waivers. In two recent decisions, the United States Court of Appeals for the Second Circuit and the Court of Appeal for the Fourth Appellate District of California held that DOJ's practices were not only coercive, but also violated the legal and constitutional rights of corporate employees, officers, directors, and agents.

On the same day that DOJ issued its revised policy under Filip, the Second Circuit handed down its decision in *United States v. Stein*, ___

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F.3d ___, 2008 WL 3982104 (2d Cir. 2008), in which the court upheld the lower court's decision to dismiss indictments against 13 former partners and employees of the accounting firm KPMG, LLP. The case stemmed from one of the largest tax fraud investigations ever conducted by DOJ. Encouraged by the fallout of widely publicized cases such as Enron, Adelphia and WorldCom, DOJ took particularly aggressive measures in investigating the activities of KPMG and its employees.

As with many governmental investigations, DOJ's policy in determining whether it would indict a corporation was largely influenced by the corporation's level of "cooperation" with the government during the investigation. In the case of KPMG's investigation, DOJ policies influenced KPMG not only to turn over all of its privileged communications with counsel, but also to severely limit the funds that it could use to pay the legal bills of former employees under investigation. The result, according to the court, was a substantial interference with KPMG's property rights and an unconstitutional interference with the 13 defendants' Sixth Amendment right to counsel.

In addition, the Second Circuit stated that "KPMG faced ruin by indictment and reasonably believed it must do everything in its power to avoid it. The government's threat of indictment was easily sufficient to convert its adversary into its agent." Thus, the court concluded, through its coercive tactics, DOJ made KPMG an unwilling participant in what amounted to a "state action" against the individual defendants. The only redress sufficient to cure such a constitutional violation was outright dismissal of the 13 indictments.

Shortly before the *Stein* decision, the Court of Appeal for the Fourth Appellate District of California issued its decision in *Regents of the Univ. of California v. San Diego County Superior Court*, 165 Cal.App.4th 672 (Cal.App. 4 Dist., 2008). At issue in this case were the civil ramifications from similarly aggressive tactics brought to bear by DOJ during the course of a governmental investigation. At the outset, a group of energy suppliers had been under investigation by a federal Corporate Fraud Task Force related to allegations that they illegally influenced the retail price of natural gas in California. Several governmental agencies (DOJ, FERC, CFTC and SEC) issued subpoenas in conjunction with this investigation and, under DOJ's policy related to its investigation, DOJ took into account the corporations' level of cooperation, including their willingness to waive the attorney-client privilege and the protection of the work product doctrine. The corporations agreed to release such information, but did so pursuant to an agreement with the government that disclosure of such information was not a waiver of the privilege or work product protections. Although the corporations were never indicted, several of their employees made plea agreements with the government.

In a later antitrust case, counsel for the plaintiffs demanded that all documents associated with the Task Force investigation be produced and that all attorney-client and work product protections associated with those documents be deemed waived. The trial court disagreed, however, and ruled that the privilege had not been waived because the documents were produced as a result of coercion, which is an exception to the waiver rule under California Evidence Code, Section 912(a). Plaintiffs countered that the defendants' decision to release such documents was a business decision and, therefore, the waiver was a knowing and voluntary relinquishment of the relevant protections. Both the underlying and appellate courts disagreed, however, and held that a waiver cannot be directly or indirectly compelled, and that the government's policy in requiring a waiver in order to gain favor during an investigation was, as a practical matter, more coercive and powerful than a court order. The court went on to state that the nature and fact of the penalties for not complying with the government's "request" could not seriously be doubted, citing *Stein* in support. Under these circumstances, the court held that no waiver had occurred.

The lessons learned from these recent events is that while the government may no longer have *carte blanche* in its investigative tactics, clients must take reasonable steps in considering whether to relinquish the privileges associated with documents. In addition, reasonable steps should be taken to protect from waiver of those privileges as to third parties or unrelated litigation. Of course, it remains to be seen if prosecutors will change enforcement practices in any way that seriously impacts a corporation's decision to waive the privilege in the course of a government investigation.

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* The Thompson Memorandum was named after its author, Deputy Attorney General Larry P. Thompson.