WHITE-COLLAR DEFENSE

TWO BIG ISSUES ON THE MINDS OF WHITE-COLLAR DEFENSE ATTORNEYS THIS SUMMER ARE whistleblowers and wiretaps. Under the Dodd-Frank Act's new whistleblower provisions, companies are hustling to compete with the U.S. Securities and Exchange Commission's generous bounty for whistleblowers. Companies are incentivizing employees to handle problems internally by cultivating a culture of compliance through robust reporting systems and bonuses.

Our panel of experts from Southern and Northern California discusses these issues as well as wiretaps, the new UK Bribery Act, and health care fraud. They are Terree Bowers and Judge Stephen Larson of Arent Fox; Ken Miller of Biernert, Miller & Katzman; George D. Niespolo of Duane Morris; Tom McConville of Orrick, Herrington & Sutcliffe; and Jim Sanders of Reed Smith. The roundtable was moderated by *California Lawyer* and reported by Lauria Schmidt of Barkley Court Reporters.

EXECUTIVE SUMMARY

MODERATOR: How are the SEC's new whistleblower provisions—including internal compliance and employee rights—under the Dodd-Frank Act impacting your practice?

BOWERS: It's even more important now for companies to get their compliance programs in order because of this outside incentive for employees to forego the internal process that might be set up to ferret out fraud. You've got to provide incentives to your employees to keep it internal, initially, rather than running straight to the outside and claiming the bounty.

SANDERS: Over the past six months, in-house counsel has grown more concerned about whistleblowers. Suddenly everybody's saying, "We want to get this done because we don't want to have a whistleblower beat us to the SEC." It has forced companies to speed up their investigations.

If you're involved in wrongdoing, you can't be the whistleblower. But if a company lawyer comes out and interviews you, and because of the interview you realize that you were on the edge of something that was illegal and suddenly the light bulb goes on that "I can be a whistleblower," this increases the danger for corporations that people who are interviewed during an internal investigation will realize that they can make a report to the SEC.

McCONVILLE: As part of augmenting existing compliance programs, companies can educate potential whistleblowers—which could be anybody in the company—that the benefits for being a whistleblower will still flow to that person if they report to the company first. Because of the way Dodd-Frank is written, the whistleblower can get the benefit of the company's internal investigation.

MILLER: Under the SEC's rules, the reward may actually increase if the whistleblower first goes through the internal-compliance program. So, just educating workers is going to be important. I see this as having a huge impact on all of our practices because there is such an incentive for folks to go to the SEC as soon as they realize there is something wrong; rather than work with the company to fix it. Because of the incentive to go straight to the SEC, it's really important that a potential whistleblower know that she can do better if she works through her employer's system.

NIESPOLO: An additional concern is that this provision and these huge award percentages could apply to related litigation. If you end up with a DOJ case, the incentive payments could also apply to those cases, not just the SEC matter.

As with qui tam actions, the monetary incentives can make people come in and try to find a way to qualify under those provisions and go to government regulators rather than first to the company. It is unfortunate that if something happens to a company with the perfect compliance plan that it was not able to prevent, it's stuck.

BOWERS: The compliance strategies before the whistleblower provision still apply. You have to make sure it's viable and vibrant, with a record of addressing fraud and problems. Hopefully, the SEC regulators will take your prior history into account when evaluat-

ing the company's conduct, if a company gets into a situation where someone bolts to the outside.

The SEC has helped clarify who qualifies as a whistleblower. If it's within your duties and responsibilities to perform compliance functions within the company, you're not going to be able to be a whistleblower. So at least you don't have your compliance officer resigning and making millions on a whistleblower suit.

NIESPOLO: Has anybody thought about talking to corporate clients about the possibility of incentivizing employees monetarily, similar to the whistleblower statute, if they come forward and report violations internally? It's just a thought.

MILLER: It's a lot in how you do it. You could incentivize somebody to come forward within the company. But you couldn't say, "We will give you money if you come to the company, but don't go to the government." Because the whistleblower can later go to the SEC, they're not actually losing anything by reporting internally and helping the company get ahead of the problem. I don't see anything wrong with it in principle.

BOWERS: The real problem is playing to mercenary interests. There's no way you're going to match the rewards the government can offer. The people who are really going to be interested are the people that are going to go to the government anyway. That's why companies really have to focus on building the culture of compliance: "You're part of this company. We truly appreciate what you have done for us, and you're going to be promoted. We want you here for the rest of your career." Then you're playing to the type of person you want in the company in the first place.

MILLER: The monetary incentive idea would be to keep people from going to the government first, just to allow the company to get ahead of the curve. Information is really important, and knowing what's going to happen would be really valuable.

BOWERS: You've got to get the internal investigation sped up and done more quickly. If you can report it to the agency first, you ice all of the potential whistleblowers.

SANDERS: Things that might have dragged out for six months in the past, now everybody's saying you've got to get it done by Tuesday because of the whistleblower issues.

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McCONVILLE: Because of that dynamic where the company wants to get out in front of it and do the investigation, and wants to report it more quickly to the SEC, you would presume that the SEC's going to get more referrals. The flip side of that is that the SEC is estimating that they're going to get 30,000 more whistleblower complaints annually. What's going to happen at the SEC when it gets inundated with thousands of potential compliance issues? It will be interesting to see if a bottleneck develops because of the whistleblower provision.

NIESPOLO: Something like monetary compensation could be part of a plan to say, "We encourage our people to come to us, and this is just another way for us to do it." It's not helpful to the company if the first time it hears about something inconsistent with its policy is when it gets a grand jury subpoena.

LARSON: It's absolutely critical for companies to get the word out that it's in everyone's interest—both for employers and for employees—that potential whistleblower's pursue internal compliance first. If the goal is to bring about compliance, as opposed to simply generating fines and litigation, there is no question that internal reporting should be the first step. From a company's perspective, it should encourage potential whistleblowers to first report internally and try to obtain compliance by providing legally appropriate incentives and ease of reporting.

McCONVILLE: I haven't thought about whether you could put in place some monetary incentive, but one concern would be is an aggressive prosecutor going after the company for some sort of obstruction of justice charge because it has in place something that could inhibit the ability of the whistleblower to report potential violations.

BOWERS: That's a real danger, particularly, let's say somebody comes in and reports something, you give them a bonus, and then you take a look at it, and it doesn't, in your view, seem to be serious enough to report it to the government. You don't report it, and later on something else happens, the government comes and looks at the history of the company, and it turns out that you have three or four instances of having paid a bonus and not reporting misconduct. You're in a heap of trouble.

MILLER: At a minimum, you would have to make sure it's clear and in writing that accepting the bonus does not prohibit the whistleblower from also going to the government. You probably also want to give them notice if the corporation is not going to report the complaint to the SEC, so they can do it themselves. Of course, such notice could also undercut the value of the program by encouraging people to take the company's reward with the full intention of also going after the SEC's reward (even if the company fully addresses the alleged problem).

NIESPOLO: Those are all good points. I'm just talking out loud about how we keep people compliant—or combat the desire not to comply given the incentives that are in place—in what we hope are good corporate businesses that would respond appropriately if they had this information upfront, and would probably go to the government in any event. There are going to be unusual situations, but maybe it doesn't work.

SANDERS: Some of these compliance programs where you're training people about the whistleblower provisions are a double-edged sword. While you're training them about the whistleblower provisions, you're also training them about how to be a whistleblower.

LARSON: A lot of it has to do with the company culture. The question is why do people report outside? I think an employee who feels that the company is doing something wrong would instinctively go to somebody within the company whom he or she could trust, as opposed to the government; that trust needs to be fostered and encouraged. I believe that can be done in a way that puts the company in a good light with the government investigators, and not a bad light.

NIESPOLO: There are studies that claim in qui tam cases a high percentage of ultimate whistleblowers first went to their company, received no response, and then they went somewhere else. We haven't seen enough of these particular cases to be able to say anything like that just yet.

BOWERS: Sometimes you have a good compliance program, but an individual cannot get through a particular supervisor to get the complaint to someone who can handle it. Either the supervisor doesn't appreciate it, or the supervisor's fully aware of it and doesn't want his or her own career damaged. You're seeing more compliance mechanisms to allow the individual employee to get around the supervisor and go to the compliance officer, and the compliance officer goes straight to the board. You have to develop an escape valve in case you've got someone with authority squelching the bad news.

MILLER: On this double-edged sword issue: Can you have a solid compliance program if you're not educating people about whistleblowers and what their rights would be?

SANDERS: I don't think you need to tell everybody there's a whistleblower provision as a part of the compliance program. But when senior management people say, "Tell us what our liabilities are," you talk about the whistleblower provisions and how it works. It would seem a little suspect to me to have two different types of programs, one where you tell upper-level management that this is what the problem is and about the whistleblower issue, and one where you don't mention the whistleblower issue to lower-level people but only tell them, "Here is how you report internally." I don't think you are required to tell them. And I don't think it's a necessary part of a program, but it's a natural part of the

program that you just have to talk about these various issues.

BOWERS: If your company comes under scrutiny and you're not informing your employees of the whistleblower provision, it looks bad. I think you've got to disclose it, but you don't have to emphasize it. That's the time you say, "We want you to come to us first. We're committed to you, so you should be committed to us. We want to address these things as quickly as we can."

SANDERS: Going back to SEC issues. You're going to have internal reporting scenarios where employees go to an independent person and report their complaints, and they have got to do something because otherwise it's just like sending the letter to the SEC. When I was regional administrator we probably had 25 letters a day from people complaining about various things. They got a really nice letter back and then there was limited follow-up. The review process was pretty cursory. If people send a letter in and they think that nobody's following up, then they're more likely to be a whistleblower.

BOWERS: A lot of times complaints really don't raise a serious issue, but you still have to address them and not let them fester.

MODERATOR: What impact will ruling on the use of wiretaps in recent fraud prosecutions, such as the Galleon case (*United States v. Raj Rajaratnam et al.*, 09 Cr. 1184 (S.D.N.Y. superceding indictment filed Feb. 9, 2010)), have on your practice?

SANDERS: My practice is mostly SEC defense, and I felt very confident over the years when people came in and asked, "Do you think my phones are bugged at home?" and I would say, up until the recent case, "Are you kidding me? They don't have the resources to do this, and it's the SEC. You might have to worry about somebody wearing a body recorder, but you don't have to worry about a wiretap." I always felt pretty confident with that, and now I give people different advice.

BOWERS: White-collar prosecutors will find that it can be a double-edged sword. Sometimes you can get very useful evidence listening in on somebody's phone, but very stringent requirements come with wiretaps. You've got to show that: more traditional law enforcement techniques have proven to be unsuccessful; report to the judge consistently; minimize the wiretaps so that you don't turn yourself into a voyeur; and protect the attorney-client privilege. There are a lot of ways to mess up a viable wiretap, which can end up in having the evidence suppressed, or discrediting the particular office that handled the wiretap.

Wiretapping will be somewhat limited because of the huge investment of resources. It's only going to be in the really large cases where you see wiretapping and the more aggressive law enforcement techniques.

NIESPOLO: The Galleon investigations have found their way into California as a result of these wiretaps. As a practical matter, analysts, advisors, and people at hedge funds are all of this mind: No one's talking on the phone. Everyone in the industry thinks their phones are tapped, their offices are bugged, everything is bugged. The fear becomes a difficult one for us to discuss with our clients.

Over the years, wiretaps were most often used in drug or OC cases, and now they're used here, not specifically for finding insider-trading violations, because that's not a listed offense authorizing a wiretap under Title III, but rather the government is saying that they're looking for wire fraud offenses. Then, as in the *Rajaratnam* case, they use the calls to prosecute the insider trading cases.

It poses a real problem to try to discuss with clients the likelihood of whether they're being tapped and where the government is going with these cases. In general, there is this huge gray area in insider trading cases about whether or not the information is material, and whether or not they can prove that trades were done on the basis of the information.

> ***"This will have a huge impact on all of our practices because there is such an incentive for folks to go to the SEC."***
>
> —KEN MILLER

Now, wiretap plus witnesses seems to equal conviction. So, the already strong incentive of white-collar defendants to work out some deal with the government, just increases in these cases as a result of their using wiretaps.

LARSON: I think the reality of the FBI and other agencies using wiretaps in these types of cases will be relatively short-lived. In the two cases I am aware of in California where a wiretap was used, they were essentially abandoned after one month. The classic wiretap involving a drug-related cartel lends itself to being a reliable source of evidence. But you're dealing with an entirely different type of target in public corruption and white-collar cases. It's a lot less likely that you're going to get the kind of evidence over the long-term that you get in the drug-related cases, and the wiretaps are also very expensive and difficult to obtain.

The perception, however, has sent shock waves through the white-collar community, and many executives are definitely wary about using their phones. And I think this fear will certainly long outlive the reality of wiretaps being used in this area.

McCONVILLE: Wiretaps have been used typically in drug cases and organized crime cases, and those prosecutors and agents are going to be different from those who are going to be pursuing mail and

wire fraud type charges.

From the government's perspective, there's an investment of time, resources, and energy for folks who have not typically engaged in that sort of investigation. It will take a while for those types of agents and prosecutors to get up to speed on wiretaps. As a practical matter, there should be very few of these.

In terms of our practice, if there is a wiretap, unlike in drug cases, there will be a civil use of the recordings. In a fraud case you could have a parallel civil case. In the *Rajaratnam* case you had a parallel SEC investigation where the recordings were potentially useful.

MILLER: Psychologically this has a huge impact because our clients are going to be thinking they're being bugged all the time. But I also think it's going to be big because, as we saw in the *Rajaratnam* case, the tapes can be very persuasive to a jury.

I appreciate the legal and practical hurdles—all the agents and resources required. But in cases with losses to victims (or potential gains to the government) in the billions of dollars, there's a huge incentive to do it.

To a certain extent, the investigation becomes a moneymaking venture. If you look in the health care industry, the government has earned billions of dollars through settlements. There's a huge incentive for the government to go forward and use these as much as they can.

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>
> —GEORGE D. NIESPOLO

MODERATOR: How have health care fraud investigations changed under the Obama Administration?

MILLER: The government is really ramping up health care fraud investigations. They have doubled the enforcement budget. They're no longer just going after Medicare fraud in Medicare Part A (Hospital Insurance) and B (Medical Insurance), but they're now going after Part C (HMOs) and Part D (prescription drugs). The False Claims Act has also been amended to make it easier for whistleblowers to bring a claim without government intervention.

For a while now, there has been a focus on getting big settlements from pharmaceutical companies. But there were complaints that pharmaceutical companies were treating such settlements as a cost of doing business. So now they are also bringing criminal charges against individuals, and trying to debar (*i.e.* exclude) individuals from federal contracts.

BOWERS: The health care industry is really under a federal siege right now. We've had cyclical focus on health care fraud, but now it is a priority connected to the president's health care reform. It has cabinet level importance. I'm sure the attorney general is briefed on it regularly. It's viewed as a panacea for the budget woes, and for financing the health care reform.

I haven't seen a single health care report out of DOJ yet that didn't highlight the recovery of millions and millions and millions of dollars. That's a function of the perceived need to justify the resources. You have the HEAT initiative, coordination between Health and Human Services and the Department of Justice, and all the different alphabet soup of auditors. You're seeing an unprecedented devotion of resources and cooperation. And you have to have results.

Health care professionals are walking around with targets on their backs. The government is looking at billing activities in Medicare to see if there are any anomalies based on what's going on in your particular region. You've got to have your own internal auditing system to make sure you're not showing up on the radar of the federal government. And if you do, you better have your backup documentation. It's no time to be sloppy.

McCONVILLE: Auditors will look to see which particular ICD-9 code, or medical procedure, is being over billed in a particular region. They do an audit to figure out who's the statistical outlier, then they request your records, and now they have the resources not just to request the records, but actually review them, follow up, and conduct interviews.

DOJ is constantly going back to Congress, saying look at the return on investment that you are getting. With additional resources for fraud prosecutors, your return on your investment will continue to grow. It's actually been a much more efficient prosecution under the Obama Administration.

LARSON: What is the goal of law enforcement in health care fraud? To me, it's getting companies to be compliant. To achieve compliance, there is a need for consistency and certainty. That is what is lacking in the new regulations, and certainly lacking in the FDRA, particularly with respect to false claims actions. I'm really concerned about the direction regulation is heading. I don't think it's good for the pharmaceutical or health care industry, and it's not good for law enforcement. The lopsided focus on punishment, forfeiture, and recovery, as opposed to compliance, is sending the industry into disarray. And I don't think it accomplishes what we really want to accomplish here, and that is eradicating health care fraud.

NIESPOLO: I totally agree with that and think that this mentality is not limited to just the health care arena. You see it in a number of the different areas where government regulation-enforcement seems to be the focus. It's not that the two are mutually exclusive, but it seems the government's preference is weighing heavily in favor of punishment versus compliance.

MODERATOR: What are your thoughts on the expanded scope and direction of the Foreign Corrupt Practices Act, and the UK Bribery Act, which went into effect July 2011?

McCONVILLE: The United Kingdom is more in lockstep with the United States under the FCPA, but the bribery provisions that the UK has promulgated are actually, in some instances, broader.

For example, whereas under the FCPA there's a defense for making facilitating payments to a government entity, there's no such exception under the UK bribery provisions.

While the FCPA is focused on briberies of foreign officials, the UK bribery provision actually sounds more like an honest services fraud type of language, because it focuses on criminalizing just the bribing, regardless of whether a foreign official is involved.

It shows what we have heard about for the last ten years, that there's a global push to stamp out corruption. This is the UK's manifestation of that global goal.

NIESPOLO: There are some defenses to the strict liability provision of the bribery statute with regard to corporations. There is an "adequate procedures defense," which states that if you have an appropriate compliance plan in place, and have taken the steps necessary in an attempt to prevent this kind of conduct, that could provide you with a defense if it's an isolated incident, et cetera. This really is something that they're very concerned about in the UK.

BOWERS: In the FCPA area it's also important to have a vigorous compliance program, a mechanism to react quickly to these allegations, and take remedial action. But again, it's become much more complex.

We have a case right now where it's a British company, but an American officer authorized the questioned conduct. So now we're under both statutory frameworks and have to deal with parallel proceedings.

SANDERS: The interest level in the implications of the Bribery Act is very high. Most firms offer video and telephone conferences on the Bribery Act to clients as it's moved forward, and for us, the response from corporate clients is higher than anything else. Rather than your partners and three people on the phone, you've got 200 responses.

MILLER: My understanding is that the law applies to any associate of any company that does business in the UK, which could include a company's employees, it's subsidiaries and maybe even its subcontractors and suppliers. It has explicit extraterritorial application, so it can reach these folks wherever they are located. Unlike the FCPA, it criminalizes commercial bribery, as well as official bribery. The statute is really amazingly broad.

How does that sit with American companies to have a law emanating from the UK that is broader than the U.S. law that will potentially suck clients into litigation overseas?

NIESPOLO: My expectation is that a lot of foreign companies are saying, "And how does it feel?" to the United States. It's been happening to them for a long time with regard to the FCPA and antitrust.

McCONVILLE: Another parallel to the FCPA is the government's promise: "You'll be cut some slack if you voluntarily disclose." Just like the FCPA, they're encouraging companies to come in and self-report, but there's no assurance that you're going to receive some quantifiable known benefit for self-reporting.

Historically FCPA cases result in settlement, but we're seeing individuals and companies challenging the government at trial. And the result is we're actually getting some case law interpreting what it is that the FCPA should apply to, and in some instances, the courts telling the government that it got it wrong.

LARSON: The increasing enforcement actions against individuals, as opposed to entities, are significant. The feds are also expanding the types of industries they're going after. And all the uncertainty in so many of these regulations and statutes makes it very difficult for individual corporate executives to know what they should be doing. In the context of our current economic struggle, the implications go well beyond law enforcement, and will have a profound effect on world economies and international relations. We're really getting into uncharted territory.

NIESPOLO: We're dealing with really, really huge numbers with corporations paying hundreds of millions of dollars when you combine fines with resolutions and class actions or civil settlements. You're seeing more and more joint investigative efforts between countries. China just passed bribery statutes, and they're setting up a whole process to do their own FCPA-like enforcement in a big way. The costs are bigger, the cases are more complicated, and the applicable laws are becoming more complicated.

MILLER: The direction of Foreign Corrupt Practices Act right now is increased individual enforcement. That's leading to more decisions, and will give clarity on some real basic issues for the FCPA that are going to provide the guidance companies need. For example, the definition of a foreign official under the FCPA is not clear. Does it extend to the state-owned entities? Or subsidiaries? The good coming out of these individual prosecutions is some clarity on what this means. ■