AN A.S. PRATT PUBLICATION
MARCH 2016
VOL. 2 • NO. 3

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Library of Congress Card Number:

ISBN: 978-1-6328-2705-0 (print)

Cite this publication as:

[author name], [article title], [vol. no.] PRATT'S GOVERNMENT CONTRACTING LAW REPORT [page number] (LexisNexis A.S. Pratt);
Michelle E. Litteken, GAO Holds NASA Exceeded Its Discretion in Protest of FSS Task Order, 1 PRATT'S GOVERNMENT CONTRACTING LAW REPORT 30 (LexisNexis A.S. Pratt)

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An A.S. Pratt® Publication

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630 Central Ave., New Providence, NJ 07974 (908) 464-6800
www.lexisnexis.com

(2016–Pub.4938)

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Corporations as Whistleblowers: Leveraging Corporations to Fight Corporate Crime

By John R. Marti and Alex Hontos*

Slowly and surely, Congress and federal agencies are pressuring corporations into becoming part of the government's team combating corporate crime. In this article, the authors address the following questions: how did we get here, why the change, and what could come next? Understanding these questions is critical for organizations and their counsel as they assess where to invest compliance resources, how to respond to government inquiries and whistleblower complaints, and, more fundamentally, how to measure risk in the new investigate-and-disclose environment.

Over the past decade, the Department of Justice has obtained record breaking criminal and civil settlements targeting corporate misconduct. This success has not, however, been matched by successful prosecutions of corporate officers. The result—fierce political and public criticism.[1] The Department's reaction to this pressure is not new or revolutionary but exhibits a return to a longstanding strategy—leverage defendants into cooperating against other defendants. Yet this strategy comes with a twist—now the Department is leveraging corporations into cooperating against their officers and employees and thereby shifting more of the burden for investigating corporate crime, including the conduct of corporate employees, onto the backs of corporations.

BACKGROUND

Throughout our country's history, a natural person was under no obligation to incriminate himself by voluntarily telling law enforcement about his own

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[1] *E.g.,* Russell Mokhiber, *The Failure to prosecute corporate crime undermines U.S. justice*, Reuters (April 30, 2013), http://blogs.reuters.com/great-debate/2013/04/30/the-failure-to-prosecute-corporate-crime-undermines-u-s-justice/.

misconduct.[2] A corporation historically was understood to be a private enterprise with many legal attributes of a natural person. As such, a corporation was generally under no affirmative obligation to disclose its own criminal conduct.[3] If a corporation's agents engaged in misconduct, the corporation would conduct an internal investigation to identify the scope and nature of the misconduct but, like a private citizen, it did not have to share that information with the government. If a corporation disclosed its misconduct, it would incriminate itself and possibly its employees. If the corporation did not self-disclose, there was limited risk that the government might discover the misconduct. In evaluating the costs and benefits, the corporation might remain silent hoping misconduct would not be discovered before the statute of limitation expired.

Congress and regulatory agencies have attempted to influence a corporation's decision in favor of disclosure. Congress has used a carrot-and-stick approach, enacting statutes to add severe criminal, civil and administrative penalties, and collateral consequences like suspension and debarment from receiving government contracts or assistance funds that are the corporate equivalent of the death penalty, while creating incentives for corporations to self-disclose. The Department of Justice and other agencies have also issued internal policies hoping to do the same.[4] The goal of these strategies was to pressure corporations to self-disclose misconduct before a government investigation started. Pressuring self-disclosure has become a key element in the government's strategy in combating corporate crime.

The result—corporations that relent to the leverage and seek "cooperation credit" by self-incriminating may mitigate or avoid severe penalties. Corpora-

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[2] *E.g.*, *State v. Wilson*, 80 Vt. 249, 67 Atl. 533 (1907) ("Mere neglect to inform the proper authorities of the commission of a crime and the identity of the felon is not in itself an offense, but such conduct becomes indictable only where the failure to report is coupled with an 'evil motive' to obstruct justice.").

[3] *Trustees of Dartmouth College v. Woodward*, 17 U.S. 518, 636 (1819) (Marshall, C. J.) ("A corporation is an artificial being, invisible, intangible, and existing only in contemplation of law . . . ."); *Marbury v. Brooks*, 20 U.S. [7 Wheat.] 556, 5 L. Ed. 522 (1822) (Marshal, C.J.) ("It may be the duty of a citizen to . . . proclaim every offense which comes to his knowledge; but the law which would punish him in every case, for not performing this duty, is too harsh").

[4] Over the past 25 years, the Department of Justice has issued numerous internal policies attempting to enhance the Department's leverage in combatting corporate crime while avoiding corporate push back for over aggressive law enforcement—particularly as law enforcement has sought access to corporate internal investigations protected by privilege. Jim Letten and Carol Montgomery, *The Yates Memo: What New Challenges To Expect*, January 3, 2016, http://www.law360.com/articles/738741/the-yates-memo-what-new-challenges-to-expect.

tions that chose to conceal or not disclose the misconduct may face draconian penalties. The government is offering bounties to employees with knowledge of the misconduct to turn in their employers. A corporation that adopts a strategy of remaining silent succeeds only if the misconduct remains undetected, and this has become a very risky strategy.

Incentivizing corporations to voluntarily self-incriminate is now a key enforcement strategy for federal corporate prosecutors. In 2015, the Deputy Attorney General of the Department of Justice, Sally Yates, instructed federal prosecutors to "leverage resources" in combatting corporate criminal conduct by pressuring corporations to incriminate themselves prior to the government becoming aware of possible misconduct, and by encouraging corporations to become whistleblowers against their employees.[5]

Yet a corporation is vulnerable to government investigations in one way that a natural person is not. A corporation does not have a Fifth Amendment right to remain silent.[6] Once the government becomes aware of corporate misconduct, prosecutors may subpoena the corporation to produce the incriminating information. As the Supreme Court noted, "[t]reating corporations as natural persons under the Fifth Amendment would have a detrimental impact on the Government's efforts to prosecute 'white-collar crime,' one of the most serious problems confronting law enforcement authorities."[7] Simply stated, a corporation can be compelled to tattle on itself and its employees. Slowly and surely, Congress and federal agencies are pressuring corporations into becoming part of the government's team combating corporate crime.

How did we get here, why the change, and what could come next? Understanding these questions is critical for organizations and their counsel as they assess where to invest compliance resources, how to respond to government inquiries and whistleblower complaints, and, more fundamentally, how to measure risk in the new investigate-and-disclose environment.

HOW DID WE GET HERE?

The federal government has long struggled with combatting corporate crime.

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[5] Deputy Attorney General Sally Yates Memorandum, Individual Accountability for Corporate Wrongdoing, September 9, 2015 (hereinafter "Yates Memorandum") ("These challenges make it all the more important that the Department fully leverage its resources to identify culpable individuals at all levels in corporate cases."), http://www.justice.gov/dag/file/769036/download.

[6] *Hale v. Henkel*, 201 U.S. 43 (1906). While corporations can be compelled to disclose facts, corporations may assert attorney–client privilege, and may generally not be compelled to disclose privileged material.

[7] *Braswell v. United States*, 487 U.S. 99, 100 (1988).

During the Civil War, Congress became concerned about the government's inability to counter an explosion in procurement fraud by war profiteers, mostly in the defense industry. In 1863, Congress responded by enacting the False Claims Act ("FCA"). The FCA prohibited the submission of false claims for payment where federal funds are involved. Congress incentivized whistleblowers to disclose fraud to the government by providing substantial bounties to strategically leverage whistleblowers to augment the federal government's own investigative resources.

As one court noted, Congress "let loose a posse of ad hoc deputies to uncover and prosecute frauds against the government."[8]

In the 1980s, again in response to numerous news stories about widespread fraud in the defense industry,[9] Congress encouraged prosecutors to combat procurement fraud in the defense industry through a specialized unit, the Defense Procurement Fraud Unit.[10] Congress also amended the FCA to significantly expand incentives to whistleblowers and penalties for corporate wrongdoers.[11] And the Department of Defense and Department of Justice instituted a Voluntary Disclosure Program to reward corporations that voluntarily disclosed fraud to the government with a possible mitigation of penalties, while promising severe penalties (including debarment) for those corporations that concealed misconduct.[12]

This strategy of leveraging corporations to self-disclose misconduct expanded into numerous other areas, including the Foreign Corrupt Practices Act (1977),[13] the Antitrust Division's Leniency Program (1978),[14] the U.S.

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[8] *United States ex rel. Milam v. Univ. of Tex. M.D. Anderson Cancer Center*, 961 F.2d 46, 49 (4th Cir. 1992).

[9] Final Report of the Packard Commission, June 1986 (issued after public criticism of DoD purchases of $600 toilet seats and $400 hammers), http://www.ndia.org/Advocacy/AcquisitionReformInitiative/Documents/Packard-Commission-Report.pdf.

[10] The DPFU was heavily criticized for its ineffectiveness in investigating defense industry corporations. *See* http://www.justice.gov/sites/default/files/jmd/legacy/2014/05/31/hear-j-99-56-1985.pdf.

[11] The law was again amended in 1986, again due to issues with military spending. Under President Ronald Reagan's military buildup, reports of massive fraud among military contractors had become major news, and Congress acted to strengthen the FCA. James B. Helmer Jr., *False Claims Act: Incentivizing Integrity for 150 Years for Rogues, Privateers, Parasites and Patriots*, 81 U. Cin. L. Rev. (2013).

[12] U.S. Attorney's Manual, Criminal Resource Manual Section 931 (Department of Defense Voluntary Disclosure Program), http://www.justice.gov/usam/criminal-resource-manual-931-department-defense-voluntary-disclosure-program.

[13] FCPA: A Resource Guide to the U.S. Foreign Corrupt Practices Act, By the Criminal

Sentencing Guidelines and Principles of Prosecution for Business Organizations (1991),[15] and the EPA's Audit Policy (1995).[16] In the aftermath of the Enron, WorldCom and other financial and accounting frauds, Congress enacted the Sarbanes-Oxley Act of 2002 which included disclosure and whistleblower protections.[17] In the aftermath of the 2008 financial collapse, Congress again responded by creating the Dodd/Frank Whistleblower Program (2011).[18]

In each instance, the government created incentives to encourage corporate self-disclosure and incentivize whistleblowing. But the government has not always relied upon voluntary incentives, and at times has mandated that corporations both investigate and then disclose criminal conduct before the government otherwise learns about the conduct. If the government could compel corporations to disclose incriminating information in response to a subpoena, Congress decided to compel self-disclosure in response to statute.

When the securities markets collapsed in the late 1920s because of systemic fraud, Congress established affirmative mandatory disclosure obligations for businesses and individuals who participated in the nation's securities markets. To protect investors, Congress enacted a series of securities laws with mandated disclosures designed to force companies to make public information that investors would find pertinent to making investment decisions.[19]

Division of the U.S. Department of Justice and the Enforcement Division of the U.S. Securities and Exchange Commission, November 14, 2012, p. 52 ("both DOJ and SEC place a high premium on self-reporting, along with cooperation and remedial efforts, in determining the appropriate resolution of FCPA matters"), http://www.justice.gov/criminal-fraud/fcpa-guidance.

[14] http://www.justice.gov/atr/leniency-program.

[15] Paula Desio, *An Overview of the Organizational Guidelines, United States Sentencing Commission* ("when the Commission promulgated the organizational guidelines, it . . . incorporat[ed] into the sentencing structure the preventive and deterrent aspects of systematic compliance programs. The Commission did this by mitigating the potential fine range-in some cases up to 95 percent-if an organization can demonstrate that it had put in place an effective compliance program. This mitigating credit under the guidelines is contingent upon prompt reporting to the authorities and the non-involvement of high level personnel in the actual offense conduct"), http://www.ussc.gov/sites/default/files/pdf/training/organizational-guidelines/ORGOVERVIEW.pdf.

[16] Incentives for Self-Policing: Discovery, Disclosure, Correction and Prevention of Violations, 60 Fed. Reg. 66706 (Dec. 22, 1995).

[17] 18 U.S.C.A. 1513(e).

[18] 17 CFR 240.21F-1 et seq. (the SEC provides monetary awards to eligible individuals who come forward with high-quality original information that leads to a Commission enforcement action in which over $1,000,000 in sanctions is ordered. The range for awards is between 10 percent and 30 percent of the money collected).

[19] Miller, Alison B., *Navigating the Disclosure Dilemma: Corporate Illegality and the Federal*

Congress enacted the Bank Secrecy Act in 1970 to mandate that financial institutions in the United States assist federal agencies to detect and prevent money laundering. In doing so, Congress created a duty on financial institutions to *investigate* criminal conduct.[20]

In the past decade, the federal government has broadened mandatory-disclosure requirements in the areas of procurement and assistance. When doing business with the government, Congress directed that corporations no longer have the discretion to decide whether to self-disclose.

In 2008, Congress passed the "Close the Contractor Fraud Loophole Act,"[21] which required that the Federal Acquisition Regulations be amended to "require timely notification by federal contractors of violations of federal criminal law or overpayments in connection with the award or performance of covered contracts or subcontracts, including those performed outside the United States and those for commercial items." Failure by a corporation to self-disclose could result in suspension and debarment.

In 2009, Congress enacted the Fraud Enforcement and Recovery Act ("FERA") which amended the FCA. Under the FERA, corporations that innocently obtain an overpayment of federal funds, but fail to timely report and return the overpayment, are subject to substantial damages and penalties under the FCA as "reverse false claims."[22] In 2013, on the assistance side of federal spending, the Office of Management and Budget issued its own mandatory disclosure rule which mandates that recipients of federal grants disclose "all violations of Federal criminal law involving fraud, bribery, or gratuity violations."[23]

Mandatory disclosure requirements give regulators and prosecutors leverage in discovering and investigating corporate crime. That was precisely the point. Yet the growth in disclosure incentives and mandates has not been accompanied by a growth in government investigative resources.

WHY THE CHANGE?

Complex corporate investigations require substantial law enforcement resources. Despite this reality, in at least the past 15 years, Congress and federal

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Securities Laws, 102 Georgetown Law Journal 1647 (2014) (discussing corporate obligations to disclose criminal conduct under the federal securities laws).

[20] Public Law 91-508.

[21] Close the Contractor Fraud Loophole Act, Pub. L. No. 110-252, 122 Stat. 2386 (2008).

[22] 31 U.S.C. § 3729(a)(1)(G).

[23] 2 CFR 200.113 (Mandatory Disclosures).

law enforcement have contributed comparatively fewer resources to combatting corporate crime, all during a period when corporate crime dominated the news.

Following the terrorist attacks of September 11, 2001, federal law enforcement dramatically and appropriately realigned resources to answer the international terrorism threat. By FY 2004, the FBI had approximately 500 fewer agents investigating white collar crime matters than in 2000.[24] This rapid and dramatic realignment resulted in a 40 percent reduction in case initiations for financial crimes as compared to FY 2000.[25] The second largest generator of federal white collar criminal case referrals is the Internal Revenue Service's Criminal Investigations Division, which saw a similar drop in staffing, from 3,363 special agents in FY 1995 to a projected 2,139 agents in FY 2016.[26] The Securities and Exchange Commission's staffing levels also did not keep pace with industry growth.[27]

In 2008 and the years following, while the FBI and the Department of Justice were publicly pronouncing that they were committed to prosecuting mortgage fraud, mortgage fraud was a low priority in many FBI field offices.[28] At the same time, the federal government saw exploding deficits and a severe constriction in funding.[29] A Department of Defense Office of Inspector General report in March 2008 observed that investigation of contracting fraud is one area of many "that have dropped in priority and have largely been neglected."[30] The result—the Transactional Records Access Clearinghouse ("TRAC") at Syracuse University noted that as of 2015 "[f]ederal prosecution of individuals identified by the government as white collar criminals is at the

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[24] DOJ OIG Report 05-37, Chapter 5, https://oig.justice.gov/reports/FBI/a0537/chapter5.htm#foc.

[25] DOJ OIG Report 05-37, Chapter 5, https://oig.justice.gov/reports/FBI/a0537/.

[26] IRS CI Fiscal Year 2014 National Operations Annual Business Report, page 5, https://www.irs.gov/pub/foia/ig/ci/REPORT-FY2014-IRS-CI-Annual-Report.pdf.

[27] SEC: In Brief, FY 2013 Congressional Justification, p.2, https://www.sec.gov/about/secfy13congbudgjust.pdf.

[28] DOJ OIG Report 14-12, Audit of the Department of Justice's Efforts to Address Mortgage Fraud, March 2014, https://oig.justice.gov/reports/2014/a1412.pdf.

[29] DOJ OIG Top Management and Performance Challenges Facing the Department of Justice, November 10, 2015, https://oig.justice.gov/challenges/2015.pdf#nameddest=1.

[30] Department of Defense Inspector General Growth Plan for Increasing Audit and Investigative Capabilities Fiscal Years 2008–2015 March 31, 2008, http://www.dodig.mil/IGInformation/IGInformationReleases/DoD%20IG%20March%2031%202008%20Report%20(FY08-15%20Growth%20Plan).pdf.

lowest level in the last twenty years . . . ."[31] Significantly, "[d]espite repeated claims to the contrary by top officials at the U.S. Department of Justice, the government's criminal prosecution of corporate violators has declined substantially in the last decade, falling by almost one third (29%) between FY 2004 and FY 2014."[32]

While law enforcement was being excoriated to do more to combat corporate crime and other misconduct, law enforcement agencies had fewer resources dedicated to combatting white collar crime, and fewer successes. The end result—only one top banker went to jail.[33] As one observer noted, "if . . . the Great Recession was in material part the product of intentional fraud, the failure to prosecute those responsible must be judged one of the more egregious failures of the criminal justice system in many years."[34]

Subject to intense criticism but lacking additional resources, the Department of Justice has returned to leverage—by pressuring corporations into taking on what historically has been a law enforcement responsibility and deputizing corporations as partners with law enforcement in the war on corporate crime. Corporations, and their employees, are now "G-men" too, or at least that is where the regulatory and enforcement landscape is trending.

WHAT COULD COME NEXT?

Corporate Whistleblowing

History has demonstrated that in every era involving the perception of substantial corporate wrongdoing, state and federal governments have responded by seeking more leverage. Absent a corporate Fifth Amendment privilege, the government may freely mandate that corporations tell law enforcement about internal criminal conduct, subject to available privileges. As history has demonstrated, the federal government increased incentives for disclosure. Next, governments adopted mandated disclosures. And now, with the Yates Memorandum, the Department of Justice is incentivizing corporations to become whistleblowers against their officers and employees. To

[31] http://trac.syr.edu/tracreports/crim/398/.

[32] http://trac.syr.edu/tracreports/crim/406/.

[33] Eisinger, Jesse, "Why Only One Top Banker Went to Jail for the Financial Crisis," New York Times Magazine, April 30, 2014, http://www.nytimes.com/2014/05/04/magazine/only-one-top-banker-jail-financial-crisis.html.

[34] Rakoff, Jed S., "The Financial Crisis: Why Have No High-Level Executives Been Prosecuted?" New York Review of Books, January 9, 2014 issue, http://www.nybooks.com/articles/2014/01/09/financial-crisis-why-no-executive-prosecutions/.

incentivize this behavior, federal prosecutors are holding out promises of amnesty or lesser sanctions. In effect, the Yates Memorandum has established a bounty system for corporations to whistle-blow on their employees.[35]

Splitting the Corporation/Officer Relationship

The government's pressure to leverage corporations against their employees is a similar strategy to that used to combat criminal conspiracies. Federal prosecutors have long used a threat of severe penalties to induce criminal conspirators to turn on one another. "[T]he Department of Justice views mandatory minimum penalties as an "essential" and "critical tool" in obtaining "cooperation from members of violent street gangs and drug distribution networks."[36] This argument is similar to the reasoning in the Yates Memorandum. For the first time, the Department of Justice's policy promises severe penalties in order to leverage corporations to turn on their employees in hopes of a sentencing benefit.

Furthermore, federal prosecutors may well increase suits against corporate officers under the FCA for civil damages (regardless of ability to pay). By suing corporate officers besides the corporation, prosecutors would likely inject conflict into the corporation-employee relationship, and may induce officers to cooperate against the corporation or other officers for some benefit.

Corporate Internal Investigations

Given the proliferation of mandatory disclosure requirements, and the multiplication of voluntary disclosure incentives, the time has come when corporations should assume that "internal" complaints and the facts discovered as a result of "internal" investigations will be disclosed. That is not to say that corporations will always be required to disclose and privileges may well still apply. But corporations should conduct internal investigations with the understanding that much of what is discovered and documented may end up in the hands of a prosecutor or an Inspector General or contracting officer. These pressures will affect the nature and tone of *Upjohn* warnings as well.[37]

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[35] Perhaps the Deputy Attorney General has let loose a posse of corporations acting as ad hoc deputies to uncover and prosecute frauds against the government by corporate officers and employees.

[36] Report to the Congress: Mandatory Minimum Penalties in the Federal Criminal Justice System, United States Sentencing Commission, October 2011, page 89, http://www.ussc.gov/news/congressional-testimony-and-reports/mandatory-minimum-penalties/report-congress-mandatory-minimum-penalties-federal-criminal-justice-system.

[37] *Upjohn Co. v. United States*, 449 U.S. 383 (1981) (attorneys interviewing corporate employees give the Upjohn warning—also known as the corporate Miranda warning—to the

But Newton's Third Law teaches that with every action there is an equal and opposite reaction. Corporations may find that internal investigations are complicated when corporate officers (who are necessary witnesses) refuse to cooperate knowing that the interviews may be turned over to law enforcement. For some officers, remaining silent knowing that they may lose their job may be preferable to the consequences of confessing to misconduct in an internal investigation. And even if officers do cooperate, this tension will certainly undermine the trust necessary for effective employee/employer relationships and the continuity of business operations.

More Disclosure Requirements

Disclosure requirements are waxing, not waning. Expect Congress and agencies to place additional specific duties on corporations requiring additional disclosures. Historically, creating additional and expensive law enforcement overhead costs has been a reactive strategy that has not eliminated corporate criminal conduct.

Shifting investigative responsibility to corporations, and then requiring corporations to disclose findings, is perceived as far more cost effective in an era of sequestration and continuing resolutions.

Prosecutions for Not Disclosing

Where mandatory disclosures exist, federal prosecutors might prosecute for knowing failure to disclose. Yet there is little evidence that prosecutors have pursued corporate "misprision of felony" cases.[38] Under this statute, corporations that knowingly conceal and do not disclose knowledge of a felony may commit a felony. Currently, prosecutors only occasionally charge misprision in a white collar case, and even this decision reflects not a desire to charge misprision for its own sake but as a result of plea bargaining. With more mandatory disclosure requirements, look for aggressive federal prosecutors to leverage misprision as a short cut to a successful prosecution.

CONCLUSION

We should not be surprised that the Department of Justice is pressuring corporations to whistle-blow. Because of the Department's difficulties in combatting corporate crime and its reduced resources, the Department is turning to proven strategies and techniques—whistleblowing and leverage. Yet corporations are not criminal organizations, and the key question as the

employees so that they know that the corporation, not the employee, holds the privilege).

[38] 18 U.S.C. § 4.

Department continues to squeeze corporations is whether this strategy will be effective, counterproductive, or even politically palatable. Newton's Third Law has yet to fully play out. There is certainly more to come. But for organizations currently facing a government inquiry or responding to internal allegations of misconduct, or merely trying to determine where to invest compliance resources, understanding that we have entered a new paradigm, albeit one with deep historical roots, is critical to appropriately allocating resources and assessing risk.