

## CLIENT ALERT

### DEPARTMENT OF JUSTICE REVISES CHARGING GUIDELINES TO LIMIT REQUESTS FOR WAIVERS OF ATTORNEY-CLIENT AND WORK-PRODUCT PROTECTIONS BY COMPANIES UNDER INVESTIGATION, AND ADDRESSES PAYMENT OF LEGAL FEES FOR EMPLOYEES



#### SUMMARY

On December 12, 2006, the Department of Justice released revised guidelines for use by federal prosecutors when considering whether to charge a company with a criminal offense. The revised guidelines modify particular provisions of what has become known as the “Thompson Memorandum,” issued in January 2003 by then-Deputy Attorney General Larry D. Thompson. In what is already being called the “McNulty Memorandum,” U.S. Deputy Attorney General Paul J. McNulty’s revised guidelines (1) require prosecutors to meet a four-part test establishing a legitimate need for information before they may request that a company waive the attorney-client privilege and work-product protections, (2) limit the instances in which the company’s declination of a prosecutor’s waiver request may be considered in evaluating the company’s cooperation with the government’s investigation, (3) instruct prosecutors that they generally cannot consider a company’s advancement of attorneys’ fees to employees in the charging decision and (4) establish procedural safeguards within the U.S. Attorney’s Office to assure compliance.

While a step in the right direction, the new guidelines do not represent a fundamental shift in the approach to the prosecution of a company. To make sure that they fall squarely within the new policies, companies should consider including written indemnification provisions in corporate charters, bylaws and employment agreements, thereby creating a contractual obligation to advance attorneys’ fees to employees for corporate criminal investigations.

#### THE THOMPSON MEMORANDUM

The Thompson Memo provided nine factors for prosecutors to use when deciding whether to charge a company with criminal offenses, including the company’s willingness to cooperate with the government. The Thompson Memo allowed prosecutors to request a waiver of the attorney-client and work-product protections in appropriate circumstances and instructed them that they should consider the willingness of a company to waive such protection as one factor in evaluating the company’s cooperation. Additionally, the Thompson Memo provided that

prosecutors could consider, in weighing the extent and value of a company's cooperation, whether the company advanced attorneys' fees to culpable employees and agents.

These particular sections of the Thompson Memo drew widespread criticism for creating a "culture of waiver," and represented an assault on individual constitutional rights, the attorney-client privilege and the work-product doctrine. The challenge to the Thompson Memo found footing recently in the KMPG case (*U.S. v. Stein*), in which a federal district judge held portions of the Thompson Memo unconstitutional for violating company employees' Fifth and Sixth Amendment rights. These provisions also have drawn the attention of Congress, most recently in Senate hearings headed by Sen. Arlen Specter. Senator Specter's draft bill, titled "Attorney-Client Privilege Protection Act of 2006," would preclude federal prosecutors, when assessing cooperation, from considering whether the company asserted privilege or paid legal fees for employees.

### **THE MCNULTY MEMORANDUM**

In response to this rising criticism, the Department of Justice released the McNulty Memo, which is nearly identical to the Thompson Memo except for its revisions to the sections dealing with (1) waivers of the attorney-client and work-product protections and (2) payments for employees' attorneys' fees. Each of these two provisions, along with others, is intended to assist the prosecutor in determining whether the company was cooperating with the government's investigation.<sup>1</sup>

### **MCNULTY'S NEW TWO-TIERED APPROACH TO ATTORNEY-CLIENT AND WORK-PRODUCT MATERIALS**

Under the Thompson Memo, prosecutors often routinely requested companies under investigation to waive the attorney-client privilege and work-product protection, without any real consideration of whether the information was needed. Hoping that a waiver would help to avoid an indictment, companies often felt compelled to comply.

The McNulty Memo attempts to clarify when a prosecutor may request a waiver of privilege. Prosecutors must now demonstrate a "legitimate need for the privileged information to fulfill their law enforcement obligations." The Memo further explains that "legitimate need for the information is not established by concluding it is merely desirable or convenient to obtain privileged information. The test requires a careful balancing of important policy considerations underlying the attorney-client privilege and work-product doctrine and the law enforcement needs of the government investigation."

Legitimate need is to be determined by consideration of four factors:

1. the likelihood and degree to which the privileged information will benefit the government's investigation;
2. whether the information sought can be obtained in a timely and complete fashion by using alternative means that do not require waiver;
3. the completeness of the voluntary disclosure already provided; and
4. the collateral consequences to a corporation of a waiver.

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<sup>1</sup> The McNulty Memo does not impact the Seaboard Release, the SEC's version of the Thompson Memo that defines the standards of corporate cooperation in SEC investigations.

If need can be established, the McNulty Memo requires that prosecutors first limit their request to “purely factual information, which may or may not be privileged, relating to the underlying misconduct” – information that it labels “Category I.” Such information would include “copies of key documents, witness statements or purely factual interview memoranda regarding the underlying misconduct; organization charts created by company counsel; factual chronologies; factual summaries; or reports containing investigative facts documented by counsel.”

Under the revised guidelines, “a corporation’s response to the government’s request for waiver of privilege for Category I information may be considered in determining whether a corporation has cooperated in the government’s investigation.”

The McNulty Memo allows that, if the “purely factual information provides an incomplete basis to conduct a thorough investigation,” prosecutors may request that the company provide attorney-client communications or non-factual attorney work product (designated as “Category II information”). Category II information, according to the new guidelines, “includes legal advice given to the corporation before, during, and after the underlying misconduct occurred,” and goes on to list specific items, including “attorney notes, memoranda or reports containing counsel’s mental impressions and conclusions, legal determinations reached as a result of an internal investigation, or legal advice given to the corporation.” The Memo cautions prosecutors to seek Category II information only in rare circumstances.

Significantly, and contrary to the Thompson Memo, the McNulty Memo states that a prosecutor “must not consider” the company’s decision to decline to provide a waiver for Category II information in making a decision to charge the company with a criminal offense. Having said that, however, the revised guidelines go on to state that a prosecutor “may always favorably consider a corporation’s acquiescence to the government’s waiver request in determining whether a corporation has cooperated in the government’s investigation.” In short, declining to waive Category II information is not supposed to hurt you, but waiving it is still favorably considered as a sign of cooperation during the investigation.

#### **PAYMENTS FOR EMPLOYEES’ ATTORNEYS’ FEES**

The McNulty Memo provides that another of the factors to be considered by a prosecutor in assessing cooperation is “whether the corporation appears to be protecting its culpable employees and agents.” In addressing this factor, the Thompson Memo allowed prosecutors, based upon the circumstances, to consider in their charging decision the advancement of attorneys’ fees to “culpable employees and agents.” The McNulty Memo, however, provides that “prosecutors generally should not take into account whether a corporation is advancing attorneys’ fees to employees or agents under investigation and indictment.” The McNulty Memo recognizes, as a result of many state indemnification statutes that permit companies to advance legal fees to officers and employees, that “many corporations enter into contractual obligations to advance attorneys’ fees through provisions in their corporate charters, bylaws, or employment agreements.” The McNulty Memo provides that the fulfillment of these obligations cannot be considered a failure to cooperate.

The McNulty Memo does permit, “in extremely rare cases,” a prosecutor to consider the advancement of attorneys’ fees “when the totality of the circumstances show that it was intended to impede a criminal investigation.” No real guidance is offered to define these situations, other than to indicate that “telling facts” will determine when “the corporation is acting improperly to shield itself and its culpable employees from government scrutiny.”

The McNulty Memo also allows prosecutors to ask questions about an attorney’s representation of a company or its employees, including how and by whom attorneys’ fees are paid.

## CONCLUSION

The McNulty Memo places some new curbs on a prosecutor's ability to request a waiver from a company. If nothing else, the Memo likely will serve to reduce the number of waiver requests. It does not, however, eliminate the consequences to the company for declining such a request if made. The consequences of declining a request for so-called Category I information are clear by the very terms of the McNulty Memo: the prosecutor may consider the response in determining whether the company has cooperated. The consequences of declining a request for Category II information are no less clear, only more subtle. Even if the prosecutor does not consider the denial of the request in his charging decision, the declination has an undeniable impact. A company that agrees to waive is rewarded; a company that declines is not.

The McNulty Memo prohibits prosecutors only from considering the advancement of attorneys' fees where there is a "contractual obligation" between the company and the employee (except in the ambiguously defined "rare cases"). Left unaddressed by the revised guidelines are those situations where the company wishes to advance attorneys' fees to employees, but without a contractual agreement, a not uncommon occurrence. In those situations, prosecutors might consider the company's conduct a failure to cooperate.

The McNulty Memo is a significant step, but what is really needed is the elimination of any requests for privileged materials and a prosecutor's consideration of attorneys' fees advanced to employees. Until such time, companies must be aware of the dilemma that they face even under the revised guidelines of the McNulty Memorandum. In the meantime, it can be expected that Congress, litigants and other interested groups will come forward to begin new challenges to the revised provisions of the McNulty Memo.

## CONTACT INFORMATION

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