

Automation Alley Newsletter

February 2011

New Federal Sentencing Guidelines Amendments Reward Strong Corporate Compliance Programs

In the United States, corporations and their executives increasingly are being prosecuted and punished for criminal activity. On November 1, 2010, recent amendments to the United States Sentencing Guidelines went into effect that impact the severity of punishment in white-collar cases involving corporations and their executives. These amendments will increase or reduce the severity of a corporation's recommended sentence depending upon, among other things, the strength and effectiveness of its compliance program. The stronger and more effective the program, the less severe the recommended sentence will be. Conversely, a weak compliance program – or the lack of one – will result in a harsher recommended sentence. With the start of a new year, corporations should create or strengthen existing compliance programs now, so as to help reduce the severity of the recommended punishment under the Sentencing Guidelines, and more importantly, to increase the likelihood of avoiding a charge in the first place.

Sentencing Guidelines Overview – Corporate Culpability Points

The first step in determining the severity of the punishment is to calculate the recommended sentence under the United States Sentencing Guidelines. Since companies cannot be sent to jail, punishment primarily comes in the form of onerous probation conditions and a hefty fine. The severity of the recommended fine is driven by the organization's "culpability score," a points-based system that defines culpability based upon a number of rigid factors. Some factors reduce the number of culpability points, while others increase them.

The November 1, 2010 amendments to the Sentencing Guidelines made important changes to the "culpability points" system. The Sentencing Guidelines now take a carrot-and-stick approach, increasing the number of culpability points based upon the size and participants within the company, while reducing the number of points if the company has an effective compliance program and fully cooperates early in the investigation.

For all offenses, a base fine is calculated on the facts of the case. Once the base fine is determined, it is either reduced or increased based upon the company's culpability score. All companies start with 5 culpability points. The final recommended fine could be quadrupled if the company receives 10 or more culpability points. (For example, the largest base fine is \$72.5 million, which quadrupled is \$290 million.) But, if the company receives 4 or less culpability points, then the minimum recommended fine is *less* than the base fine. With 2 or less points, the entire range of the recommended fine is *less* than the base fine.

Involvement in or Tolerance of Criminal Activity Increases Culpability Score

Companies can incur additional culpability points depending on the facts of the case, including (among other things) who was involved in or tolerated the criminal activity. Corporations with 5,000 or more employees will incur 5 points if (1) someone in upper management participated in, condoned, or was willfully ignorant of the offense; or (2) tolerance of the offense by personnel with substantial authority is pervasive. Under the same circumstances, corporations with 1,000-4,999 employees will earn 4 points, and corporations with 200-999 employees will earn 3 points. For companies with less than 200 employees, no culpability points will be assessed unless someone with substantial authority participated in, condoned, or was willfully ignorant of the offense. In other words, pervasive tolerance alone does not trigger additional culpability points for smaller corporations. If points are assessed, the Sentencing Guidelines draw another size distinction – 2 points for 50-199 employees, but only 1 point for 10-49 employees. Notably, this means that Mom-and-Pop shops with less than 10 employees cannot be assessed any additional culpability points for management's involvement in or tolerance of criminal activity.

Cooperation and Effective Compliance Programs Reduce Culpability Score

Since all companies start with 5 culpability points, larger corporations can easily incur a 10-point culpability score simply because of their size and management's involvement in the offense. For this reason, maintaining an effective compliance and ethics program is critical to reducing the company's recommended fine. Such programs can reduce a company's culpability score by 3 points. Full cooperation and early acceptance of responsibility can further reduce a company's culpability score by up to 5 points. So, for larger corporations facing 10 culpability points, implementing an effective compliance program and cooperating with the government could reduce the company's culpability score to 2 points (assuming the company has not incurred additional points for committing similar offenses within the last 10 years, for obstructing justice by impeding the investigation, prosecution or sentencing of the case, or for violating any court orders through the offense conduct). For mid-size companies facing 8 points, the culpability score can be reduced to zero. From 0-2 points, the recommended fine will always be below the base fine.

Importantly, a corporation can incur more than 10 points if it committed a similar offense within the last 10 years; obstructed justice by impeding the investigation, prosecution or sentencing of the case' or violated any court orders when committing the offense. In fact, a corporation can incur as many as 17 culpability points. In such cases, securing a reduction in culpability points through an effective compliance program and other options is essential, since there is no difference in the recommended fine after 10 points (at which point the recommended fine is quadrupled from the base fine).

Cooperation and Effective Compliance Programs May Help Avoid Prosecution Altogether

On a related note, the Justice Department's Principles of Federal Prosecution of Business Organizations direct prosecutors to consider several factors when deciding whether to indict a company. Two of those factors are (1) whether the company timely and voluntarily disclosed the offense and is willing to cooperate in the investigation; and (2) whether the company had a pre-existing effective compliance program.

In many respects, the Sentencing Guidelines' measurements of a compliance program's effectiveness overlap with the Justice Department's Principles of Federal Prosecutions of Business Organizations. This means that, even if a company's compliance program does not prevent a charge, it may significantly reduce the severity of punishment if the company is found to have acted unlawfully. Should prosecutors decide that the corporation has adopted and implemented a truly effective compliance program, they may decide (when consistent with other federal law-enforcement policies) to not charge the company, to reduce the number charges brought, or to seek lesser punishment.

Consequences of Not Having a Compliance Program

There are several consequences to foregoing an effective compliance program. First, it will increase the company's risk of being charged with a crime under the Justice Department's Principles of Federal Prosecution of Business Organizations. Second, it will result in a higher culpability score, meaning that the company will end up with a much higher recommended fine. Finally, a less well-known consequence, is that the sentencing judge can order the company to design a court-approved compliance program and submit to regular court oversight to ensure that the program is properly implemented. In other words, not having a compliance plan today means the company will likely pay bigger fines tomorrow and be forced to adopt a compliance plan anyway. Implementing one now is a smart investment for the company's future.

What Constitutes an Effective Compliance Program?

Corporate executives and counsel may wonder how a compliance program could ever be deemed "effective" if employees are caught violating the law. The Sentencing Guidelines expressly recognize that a compliance program can never prevent criminal activity 100% of the time. The new Sentencing Guidelines also take a flexible approach, permitting companies to tailor their programs to needs and nature of their business – the Sentencing Guidelines do not impose a cookie-cutter compliance program.

Effectiveness is judged by the standards and procedures that the company adopts and the company's commitment to the program, as demonstrated by the tone from the top, training programs, and day-to-day implementation. The Sentencing Guidelines also focus on whether the program successfully uncovered the problem internally before government investigators learned of the activity. Although they permit flexibility in design and implementation, the Sentencing Guidelines expect that larger companies will adopt more formalized programs. One essential feature for larger companies is the appointment of an independent ethics officer with operational responsibility for the program and with direct reporting obligations to the company's governing body or an appropriate subgroup (e.g., an audit committee of the board of directors).

How Can My Company Create (or Adapt a Current) Compliance Program?

Butzel Long's White Collar Criminal Defense, Internal Investigations, and Corporate Compliance Team can help you prepare an effective compliance program that maximizes the benefits available to your company under federal laws, regulations, and sentencing policies. Our Team routinely conducts internal investigations and advises management, boards of directors, and audit committees on establishing compliance programs, with an emphasis on the Sarbanes-Oxley Act, the U.S. Securities & Exchange Commission's *Seaboard* Principles, the Justice Department's Principles for

Federal Prosecution of Business Organizations, the Federal Sentencing Guidelines, and the newly enacted Dodd-Frank Act.

For more information, please contact our White Collar Criminal Defense, Internal Investigations, and Corporate Compliance Team.

David F. DuMouchel

Phone: 313.225.7004

Email: dumouchd@butzel.com

Joseph E. Richotte

Phone: 313.225.7045

Email: richotte@butzel.com

Damien DuMouchel

Phone: 313.225.7055

Email: dumoucheld@butzel.com

George B. Donnini

Phone: 313.225.7042

Email: donnini@butzel.com

Mary M. Mullin

Phone: 313.225.7093

Email: mullin@butzel.com

This news is only intended to highlight some of the important issues. This e-mail has been prepared by Butzel Long for information only and is not legal advice. This information is not intended to create, and receipt of it does not constitute, a client-lawyer relationship. Readers should not act upon this information without seeking professional counsel. This electronic newsletter and the information it contains may be considered attorney advertising in some states.

Attorney Advertising Notice - The contents of this e-mail may contain attorney advertising under the laws of various states. Prior results do not guarantee a similar outcome.

For previous e-news or to learn more about our law firm and its services, please visit our website at: www.butzel.com

Butzel Long Offices:

Ann Arbor
Bloomfield Hills
Detroit
Lansing
New York
Washington D.C.

Alliance Offices:

Beijing
Shanghai
Mexico City
Monterrey

Member:

Lex Mundi