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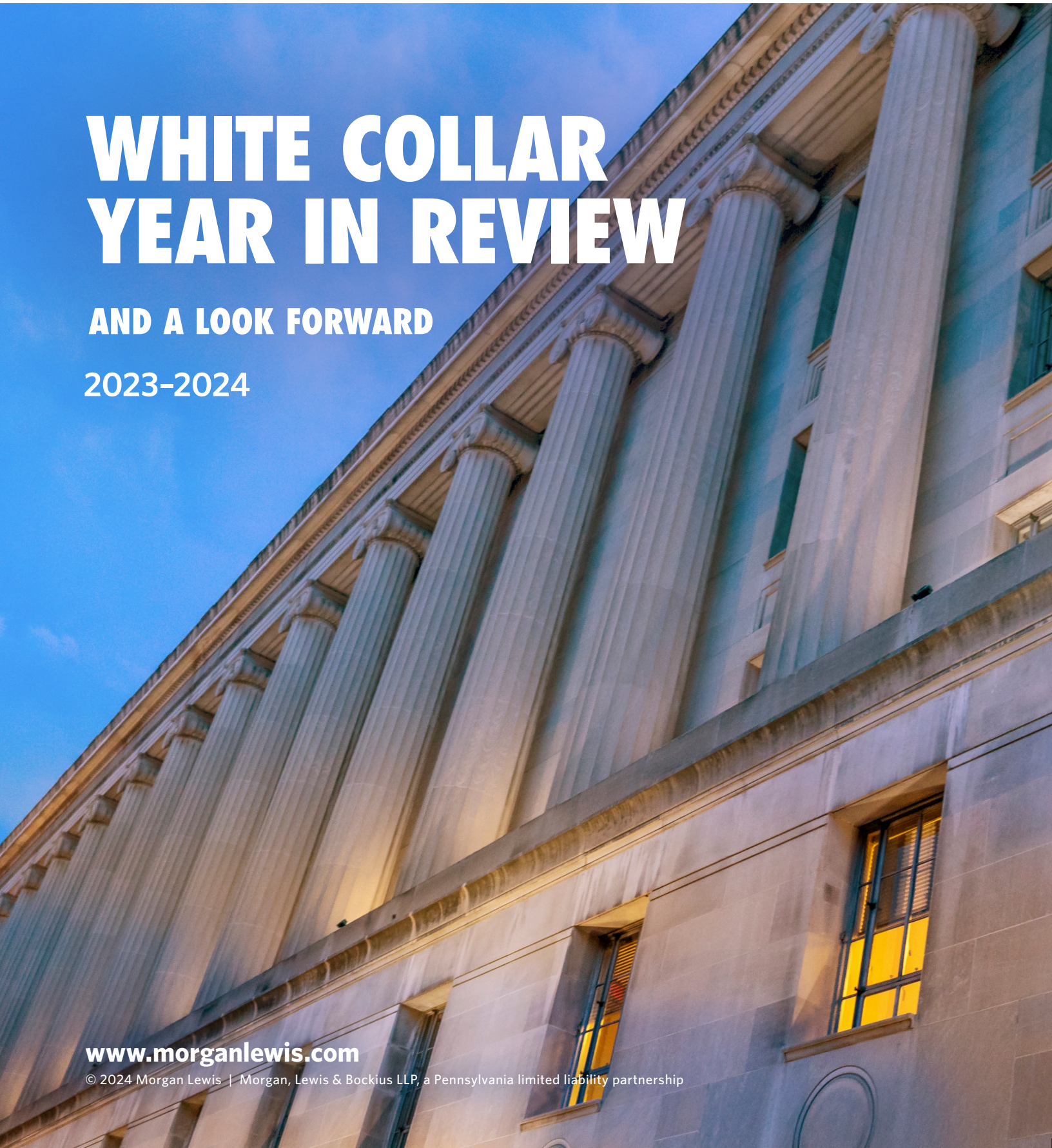
REPORT

WHITE COLLAR YEAR IN REVIEW

AND A LOOK FORWARD

2023–2024



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WHITE COLLAR: YEAR IN REVIEW AND A LOOK FORWARD, 2023–2024

The white collar world had an active year, with the last 12 months yielding further incentives from the US Department of Justice (DOJ) to encourage voluntary disclosures as well as key rulings from the US Supreme Court that have affected the False Claims Act (FCA) landscape—all of which have meaningful implications for 2024.

In this report, we highlight significant white collar milestones from 2023 and how they may shape the new year. These developments include everything from the DOJ's emphasis on the importance of due diligence in transactions to its move toward assessing businesses activities through a national security lens, to the Supreme Court's rulings on the FCA's scienter element and the DOJ's dismissal authority.

AGENCY GUIDANCE AND DIRECTIVES

2023 Highlight: Clawback Pilot Program Launched

In the spring, Deputy Attorney General Lisa Monaco announced the launch of a significant pilot program on compensation incentives and clawbacks during a speech at the ABA White Collar Crime Conference in Miami. Under the "first-ever" three-year pilot program, companies will be able to reduce criminal fines by attempting in good faith to claw back compensation from individual wrongdoers—even if those efforts are unsuccessful—and the companies will be able to retain any recovered funds.

At the time, the pilot program and the Criminal Division's Evaluation of Corporate Compliance Programs' changes were the latest, but certainly not 2023's last (as discussed below), in a line of announcements regarding new or revised policies, all of which are meant to incentivize companies to voluntarily disclose problems, to enhance their corporate compliance policies, and to punish individual wrongdoers. The pilot program is unique among these policies because it offers clear guidance on the DOJ's expectations and potentially meaningful, quantifiable benefits. Additionally, it seemingly recognizes the real-world difficulties of implementing clawbacks by crediting good faith—albeit unsuccessful—efforts to go after individual compensation. In practice, this is not a meaningful shift for regulated industries or companies with mature compliance programs that have designed and implemented financial disincentives for wrongdoers. However, for less mature organizations, this could be perceived as transformative within the organization. What is clear is that today, an important aspect of any resolution is addressing, head on, what remediation has been implemented—whether that be terminations, withholding of bonuses or promotions, voiding equity, or seeking to claw back compensation.

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> The expectation isn't that the DOJ snaps its fingers and expects you to have a fully functional clawback program. But it is expecting you to start that process.
>
> **John Pease, *Compliance Week***

Impact in 2024

In the months ahead, the defense bar will be focused on how this policy will be effectuated and in what circumstances. The DOJ specifically stated that the penalty levied in the Albemarle resolution reflected a reduction tied to this Pilot Program for the company's decision not to pay out bonuses. This is a clear indication that the DOJ is not just focused on clawbacks of compensation but is seeking to provide credit for all financial penalties levied by companies where serious misconduct exists. Companies should review their existing disciplinary matrices to explicitly contemplate financial disincentives (i.e., withholding bonuses, no merit increase, no promotability, or no equity) for serious misconduct.

2023 HIGHLIGHT: M&A SAFE HARBOR POLICY ANNOUNCED

Deputy Attorney General Lisa Monaco announced the US Department of Justice's new Safe Harbor Policy impacting mergers and acquisitions (M&A) on October 4. Through this policy, acquiring companies can avoid DOJ charges if they voluntarily disclose wrongdoing from acquired companies. Acquiring companies that can satisfy the Safe Harbor Policy requirements can qualify for a "presumption of declination" through the following criteria:

- Self-disclosure within six months: The acquiring company must disclose the misconduct at the acquired company within six months of the transaction closing date, regardless of whether the misconduct was discovered before or after the acquisition.
- Cooperation: The acquiring company must fully cooperate with the ensuing investigation.
- Remediation within 12 months: The company must fully remediate the disclosed misconduct one year from the closing date, including restitution and disgorgement. The timeline to meet the safe harbor requirements is short. However, recognizing that every M&A deal is different, this one-year deadline can vary depending on "specific facts, circumstances, and complexity of a particular transaction."

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> By identifying red flags in due diligence, "when you put your team on the ground for transition purposes, they know where they need to start digging to try and figure out whether or not there are issues that need to get fixed or get disclosed to the government to protect the longer-term interests of the company."
>
> **Zane Memeger, *CFO.com***

Impact in 2024

Companies involved in M&A should align on the M&A objectives and integration strategy in order to allow legal and compliance to perform adequate anticorruption due diligence, risk assessments post-closing, and timely integration of all internal controls (financial and anticorruption) in order to get the benefit of this safe harbor, if necessary.

To learn more about select compliance initiatives launched by the DOJ in 2023, read the Morgan Lewis and *Compliance Week* Anti-Bribery and Corruption Survey Report, which also discusses the key findings of a tailored, in-depth assessment of compliance leaders—ranging from auditors and cybersecurity specialists to chief compliance officers and general counsel—and their current practices and priorities, including their confidence in their financial controls, use of data to inform and improve their compliance functions, and understanding of the importance of third-party due diligence.

2023 Highlight: National Security Focus Underscored

Since the beginning of the Biden administration, the DOJ has loudly proclaimed an interest in increased corporate criminal enforcement in traditional white-collar spaces. However, in recent months, the DOJ has signaled an additional priority: corporate enforcement related to national security issues. In the fall of 2023, the DOJ announced the appointment of the National Security Division's first chief counsel for corporate enforcement. Ian Richardson, a former federal prosecutor in the US District Court for the Eastern District of New York, was appointed to coordinate and oversee the prosecution of corporate crime relating to US national security. Additionally, Christian J. Nauvel was named as Deputy Chief Counsel for Corporate Enforcement.

Given some of the national security issues that have emerged in recent years, from trade secret theft to the visibility of non-state actors, the DOJ is looking for opportunities to send a message to companies that they need to crack down on misconduct that could have serious national security implications. The DOJ's focus on national security extends to processes like the CFIUS regulatory process, which is focused on reviewing cross-border investments and not on criminal activity.

> "The last thing a company wants is to be caught flat-footed in a national security investigation—doing so can be bad not just for business but for the country."
>
> **Justin Weitz, *Agenda***

Impact in 2024

Companies should be aware that the DOJ is seeking to increase enforcement in this space. The DOJ will likely increase the number of investigations and subpoenas, which will increase legal costs for companies—especially companies with activities facing national security–sensitive regions such as China, the Middle East, and Central Asia.

IN THE COURTS

2023 Highlight: SuperValu and Safeway

On June 1, the US Supreme Court held that the False Claims Act's (FCA's) scienter element requires analysis of the defendant's subjective intent at the time of the alleged false claim, and that a defendant can be liable even if the underlying statute or rule is ambiguous and can be reasonably interpreted to allow the defendant's conduct. Ultimately, the government and qui tam relators still bear the burden of proving actionable scienter, which—as the Court reiterated—does not create liability for "honest mistakes." In emphasizing the fraud-based nature of the FCA and its common law origins, the Court hewed closely to its admonitions in *Universal Health Services v. United States ex rel. Escobar*, 136 S. Ct. 1989 (2016), that the statute's elements should be applied rigorously in order to prevent the FCA from devolving into an "all-purpose anti-fraud statute" that would penalize garden-variety breaches of contracts or regulations.

While a significant decision with respect to the element of scienter, it did not impact falsity, materiality and other defenses. These defenses have been and remain an important path to success in FCA cases. While the decision may make success on a motion to dismiss on scienter more difficult to achieve, the Court's holding that the defendant's subjective belief whether a claim is false at the time submitted reinforces the good faith defense. It will be even more important in light of the decision for companies to put in place mechanisms to document their decision-making process regarding compliance with ambiguous statutes, regulations, and contract provisions so that the evidence supporting this good-faith defense will be readily accessible.

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Impact in 2024

We can expect to see the DOJ and relators continue to advocate a broad reading of the decision beyond scienter, while the defense side will continue to advocate a limited reading. The district and appellate courts will also continue to grapple with the decision's "standard" for "reckless disregard" that is far from clear.

2023 Highlight: Polansky

The US Supreme Court's decision in *United States ex rel. Polansky v. Executive Health Resources* confirms the relative ease by which the US government can exercise its dismissal authority under FCA Section 3730(c)(2)(A). The decision makes clear that the government must intervene in order to dismiss but reaffirms that the standard for dismissal is very deferential to the government. What is most remarkable about the decision is that three justices invited the prospect of a future constitutional challenge to the FCA's qui tam provisions. While the holding with respect to deference to the DOJ's dismissal authority was expected, it puts the imprint of the US Supreme Court on this broad authority. As qui tams account for the overwhelming percentage of FCA actions, dismissal of the frivolous and parasitic ones would have a significant impact. We hope the decision encourages the DOJ's more active use of this authority. As to the seeming-invitation by three justices to mount a constitutional challenge to the qui tam provisions, there has never been an appetite before for the Court to strike it down—maybe this is a harbinger of change.

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Impact in 2024

The question for 2024 is if the DOJ will more actively use its dismissal power now that the Supreme Court has affirmatively confirmed the standard. Another question for 2024 is if three justices indicating a view that the qui tam provisions may violate Article II of the Constitution will encourage anyone to take up the invitation for a constitutional challenge to these provisions.

> This holding does not [effect] a sea change in the government's dismissal authority, as none of the competing standards imposed any heavy burden on the government. Rather, the issue in everyday FCA practice has been the government's rare exercise of that prerogative in cases that clearly warranted such government action. The question is whether the government will take this opportunity to actually exercise that authority in a more routine fashion.
>
> **Douglas Baruch, *Westlaw Today***

CONCLUDING THOUGHTS

Given that the past is often prologue, we are hopeful that the highlights touched on here, and our thoughts on how these developments may play out in the months ahead, provide some insight of what is in store for 2024.

In the meantime, the latest supplement of partner Douglas Baruch's *Civil False Claims and Qui Tam Actions* treatise, published by Wolters Kluwer, is now available, and we look forward to participating in the ACI's 11th Annual Advanced Forum on False Claims and Qui Tam Enforcement on January 23 to 24 in New York as well as the Federal Bar Association's Annual False Claims Act and Qui Tam Conference on February 22 to 24 in Washington, DC.

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