

Liability Without Fault: New Enforcement Trends Against Corporate Executives

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Whenever a financial crisis occurs, government investigations and prosecutions follow. After the savings and loan debacle of the 1980s, bank officers were prosecuted, usually for abetting misrepresentations in loan applications. When market timing in the mutual fund industry came to light, fund managers were investigated for permitting late trading and market timing by their investors. After a 2006 article pointed out abuses in options backdating, the government initiated investigations, enforcement actions, and criminal prosecutions based on misstatements of the basis on which options were priced in corporate documents. In each of these cases, the object of government enforcement efforts was intentional, fraudulent conduct by corporate officers and executives.

In the aftermath of the financial meltdown of 2008, the government's enforcement efforts are aimed once again at corporate officers and executives, and in many cases at intentional, fraudulent conduct. However, many current enforcement efforts and priorities are based on legal theories markedly different from those used in the past. Today, executives in public companies may face investigations and enforcement actions by the Securities and Exchange Commission (SEC or Commission) and the Department of Justice (DOJ) *where they have done nothing intentionally wrong.*

Their "fault" is to have been in charge when a violation occurred.

In the pharmaceutical industry, in response to Congressional criticism, the Food and Drug Administration (FDA) has announced its intention to bring investigations under the so-called *Park* doctrine, against company executives in positions of responsibility when a product is sold in violation of the Food, Drug and Cosmetics Act (FDCA). In at least one case, the SEC is using Section 304 of the Sarbanes Oxley Act as the basis of an enforcement action seeking a "clawback" of compensation from a CEO who was in charge when earnings were restated, despite the absence of any allegation that the CEO knew of the violation. The new Dodd-Frank law provides broader authorities aimed at recouping executive compensation without intentional wrongdoing. The Federal Deposit Insurance Corporation (FDIC) has announced that it will seek return of compensation from bank officers on whose watch a bank has failed.

These efforts test traditional concepts of individual liability for corporate offenses. In 1961, Supreme Court Justice John Harlan wrote:

In our jurisprudence guilt is personal, and when the imposition of punishment on a status or on conduct can only be justified by reference to the relationship of that status

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or conduct to other concededly criminal activity . . . that relationship must be sufficiently substantial to satisfy the concept of personal guilt in order to withstand attack under the Due Process Clause of the Fifth Amendment.¹

If Harlan's concept of personal guilt – Oliver Wendell Holmes used the term “blameworthiness”² – is to have meaning today, the application of these strict liability authorities should be questioned, at least in the criminal context, where corporate executives have indeed carried out their duties and are nevertheless held responsible for corporate offenses.

This article examines the basis for liability in such actions and discusses steps executives can take to protect against unfair assignment of blame when bad things happen on their watch.

Prosecution of Individuals in the Pharmaceutical Industry

Nowhere is the current focus on strict liability for corporate executives more apparent than in the pharmaceutical industry. For years, the government has investigated and settled allegations of off-label marketing and anti-kickback violations, in some cases reaching billion-dollar settlements with companies, without charging individuals. As a result of recent criticism of this record, the DOJ is beginning to turn to a little-used authority known as the *Park* doctrine, to reach executives in pharmaceutical companies and hold them accountable criminally for violations previously resolved only by financial settlements with their companies.

The Park Doctrine

The *Park* Doctrine, based on the U.S. Supreme Court decision in *United States v. Park*,³ permits prosecutors to charge “responsible corporate officers” when a corporation has committed a violation of the FDCA. The doctrine is based on the

theory that executives who manage companies regulated by the FDA have an affirmative duty to ensure the safety of their products.

A *Park* violation is generally thought of as a “strict liability” offense. Prosecutors need not prove that the person had intent to commit a crime nor knowledge of any wrongdoing. The executive is subject to a misdemeanor conviction if he does not exercise “the highest standard of foresight and vigilance.”⁴ Criminal liability may be determined solely based on the executive's position as a responsible corporate officer. According to the case law, although an impossibility defense may be available if an executive can show he exercised extraordinary care but nevertheless was powerless to stop the violation,⁵ this standard is difficult to meet.⁶

The *Park* Doctrine has not been used frequently since the 1970s, and it is usually applied in cases involving manufacturing practices. However, in recent years, DOJ has shown interest in using it to prosecute individuals for misdemeanor violations related to marketing practices in the health care industry. This use of the *Park* doctrine has yet to be tested in a trial.

In 2007, three executives of the Purdue Frederick Company, Inc. pleaded guilty as “responsible corporate officers” to one misdemeanor count of misbranding the drug OxyContin.⁷ While they were not sentenced to a term of imprisonment, the executives were ordered to pay \$34.5 million to the Virginia Medicaid Fraud Unit's Program, even though the government stipulated that none of the executives had any personal knowledge of the criminal conduct.

In 2009, Las Vegas-based ingredients broker ChemNutra and its owners, Sally Qing Miller and Stephen Miller, pleaded guilty to misdemeanor charges of selling adulterated and misbranded pet food.⁸ The owners were sentenced to three years of probation and ordered to pay a \$5,000 fine. In sentencing the owners, U.S. Magistrate Judge John

T. Maugher stated that “the evidence does not support the conclusion that you all intentionally imported a pet food product into the United States that you knew would kill animals. But I am also convinced on this record that you did engage in conduct in importing a product that had that consequence. And like everything we do, actions have consequences and responsibility must be borne for that consequence.”⁹

Later in 2009, Synthes, Inc., a wholly-owned subsidiary of Norian Corporation, and four of its executives were indicted for the off-label promotion of a cement bone void filler, Norian XR.¹⁰ The government charged each of the Synthes executives with a single misdemeanor count of shipping adulterated and misbranded product. They pleaded guilty as “responsible corporate officers” under the *Park* Doctrine.¹¹ Although the officers have not yet been sentenced, prosecutors are seeking jail time.¹²

Such enforcement efforts are likely to continue. Recently, the FDA issued new guidelines concerning *Park* Doctrine prosecutions. The FDA prefaced its guidelines by noting that “[m]isdemeanor prosecution under the [FDCA] can be a valuable enforcement tool.”¹³ The new guidelines state that in determining whether to recommend a misdemeanor prosecution against a corporate official, the agency is to “consider the individual’s position in the company and relationship to the violation, and whether the official had the authority to correct or prevent the violation. Knowledge of and actual participation in the violation are not a prerequisite to a misdemeanor prosecution but are factors that may be relevant when deciding whether to recommend charging a misdemeanor violation.”¹⁴ Although the FDA expressly declined to define or provide illustrations of the categories of persons that it would refer for criminal prosecution based on the *Park* Doctrine, comments that government officials have made in recent months suggest that enforcement efforts in this area are likely to increase. For example, Lew Morris, chief counsel for the Inspector General of the

Department of Health and Human Services, was quoted recently as saying “we’re targeting managers and executives who should have known.”¹⁵ Echoing these statements, Food and Drug Administration Deputy Chief for Litigation Eric Blumberg stated at an October 13, 2010 conference: “Unless the government shows more resolve to criminally charge individuals at all levels in the company, we cannot expect to make progress in deterring off-label promotion.”¹⁶

Permissive Exclusion

In addition to fines and jail time, executives convicted of a *Park* misdemeanor face exclusion from participation in federal health care programs, such as Medicare, at the discretion of the Office of Inspector General (OIG) of the Department of Health and Human Services (HHS). For example, in the Purdue Frederick case discussed above, the three convicted executives were excluded by the OIG from participation in federal healthcare programs for 12 years. This was the first time the OIG used its permissive power to exclude executives based on the *Park* Doctrine.¹⁷

On December 13, 2010, the United States District Court for the District of Columbia affirmed HHS’s decisions to exclude the former executives.¹⁸ The Court rejected their argument that they were ineligible for exclusion because their convictions stemmed only from their “status as corporate officers” rather than their own individual conduct.¹⁹ It held that, although the *Park* doctrine does not require that an executive be aware of the violation, liability extends to officials who stand in a “responsible relation” to the violation and whose “failure to exercise the authority and supervisory responsibility reposed in them by the business organization resulted in the violation complained of.”²⁰

Even if the government decides not to pursue a misdemeanor prosecution against an individual, the OIG still has authority to exclude executives from federal health care programs if they are officers or

managing employees of an entity that has been excluded or has been convicted of certain offenses.²¹ On October 20, 2010, the OIG issued guidance containing a series of nonbinding factors it will consider in deciding whether to exclude an owner, officer, or managing employee under this provision.²² Under these guidelines, owners may be sanctioned only if they “knew or should have known” of the conduct that formed the basis of the action against the company, but officers and managers may be excluded even when there is no evidence that they knew or should have known of the alleged wrongdoing.²³

On September 22, 2010, the House of Representatives passed a bill, H.R. 6130, that would further expand the OIG’s authority to debar individuals. The bill would allow the OIG to exclude not only current executives, but also officers or managing employees who *were* in their position when the company committed the alleged wrongdoing. This would allow the OIG to reach executives after they leave a sanctioned corporation.

New Enforcement Priorities of the SEC

Since the Sarbanes-Oxley Act (Sarbanes-Oxley) was enacted in 2002, in the wake of the Enron and WorldCom debacles, the SEC has had authority to pursue “clawbacks” of compensation received by executives of public companies in certain circumstances. The recent Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) adds additional enforcement tools and whistleblower incentives aimed at recovering executive compensation. In response to Dodd-Frank, the SEC has announced a proposed whistleblower program. These enforcement efforts promise new and harsh scrutiny of executives presiding over companies that experience financial difficulties.

Section 304 of Sarbanes-Oxley

Section 304 of Sarbanes-Oxley gives the SEC the authority to pursue clawbacks of executive compensation. It provides that if a company is required to prepare an accounting restatement

due to the material noncompliance of the issuer, *as a result of misconduct*, with any financial reporting requirement under the securities laws, the chief executive officer and chief financial officer of the issuer shall reimburse the issuer for . . . any bonus or other incentive-based or equity-based compensation received by that person from the issuer during the 12-month period following the first public issuance or filing with the Commission (whichever first occurs) of the financial document embodying such financial reporting requirement; and . . . any profits realized from the sale of securities of the issuer during that 12-month period.²⁴

Although the statute requires that the accounting restatement be “a result of misconduct,” it does not state *whose* misconduct creates liability. At least one court, in *SEC v. Jenkins*, has held that the misconduct need not have been committed by the defendant officer.²⁵ In reaching its decision, the District Court of Arizona reasoned that Sarbanes-Oxley’s plain meaning requires only “the misconduct of corporate officers, agents or employees acting within the scope of their agency or employment,” not “the specific misconduct of the issuer’s CEO or CFO.”²⁶ The court noted that the statute requires an issuer’s CEO and CFO to certify each quarterly and annual report.²⁷ This requirement “provides an incentive for CEOs and CFOs to be rigorous in their creation and certification of internal controls”²⁸

It should be noted that, while Section 304 was enacted in 2002, the SEC did not bring any enforcement actions under Section 304 until 2007.²⁹ Moreover, prior to *Jenkins*, the SEC limited

enforcement actions to instances in which a CEO or CFO knowingly or intentionally directed, participated in or approved of fraudulent acts or misrepresentations concerning a company's financials.³⁰ Although SEC enforcement staff seem to be showing more interest in Section 304, it is not yet clear whether *Jenkins* signals a general trend toward more aggressive use of Section 304 in the absence of any fault by a CEO or CFO.

Section 954 of Dodd-Frank

Section 954 of Dodd-Frank requires an issuer to pursue clawbacks of executive compensation in certain instances. The section provides:

[I]n the event that the issuer is required to prepare an accounting restatement due to the material noncompliance of the issuer with any financial reporting requirement under the securities laws, the issuer will recover from any current or former executive officer of the issuer who received incentive-based compensation (including stock options awarded as compensation) during the 3-year period preceding the date on which the issuer is required to prepare an accounting restatement, based on the erroneous data, in excess of what would have been paid to the executive officer under the accounting restatement.³¹

Section 954 differs from Section 304 of Sarbanes Oxley in several respects. First, Sarbanes-Oxley's Section 304 applies to CEOs and CFOs specifically. Dodd-Frank's Section 954 provides for reimbursement from all current or former "executive officers."³² Second, under Section 304, the clawback is for the "12-month period following the first public issuance or filing" of a financial statement containing misrepresentations. In contrast, Section 954 covers "the three-year period preceding the date on which the issuer is required to prepare an accounting restatement, based on the erroneous data." Third, unlike Section 304, Section 954 does not give the Commission or other

exchanges authority to exempt smaller or foreign private issuers from enforcement actions. Lastly, while Section 304 contains a misconduct requirement for triggering the clawback, Section 954 does not appear to contain such a requirement.

Although Section 954 requires issuers, rather than the SEC, to seek the clawbacks, the statute provides the SEC with authority to "direct the national securities exchanges and national securities associations to prohibit the listing of any security of an issuer that does not comply with the requirements of this section."³³ Cases under Section 954 have not yet been litigated, and the SEC recently announced that it will delay the promulgation of implementing regulations until late 2011.³⁴ The breadth of Section 954 as written, however, suggests that this provision may become a powerful enforcement tool.

New Whistleblower Incentives Under Sarbanes-Oxley and Dodd-Frank

In response to the enactment of Dodd-Frank, the SEC recently proposed rules for revising its whistleblower program. The stated purpose of the new rules is to provide a "simple, straightforward" whistleblower program "to reward individuals who provide the agency with high-quality tips that lead to successful enforcement actions."³⁵ To be considered for an award, a whistleblower must voluntarily provide the SEC with original information about a violation of the federal securities laws that leads to a successful enforcement action resulting in monetary sanctions totaling more than \$1 million.

Section 21F of Dodd-Frank authorizes the SEC to pay rewards to individuals who provide original information that leads to "any judicial or administrative action brought by the commission under the securities laws that results in monetary sanctions exceeding \$1,000,000."³⁶ This section greatly expands the SEC's authority to compensate individuals who provide the Commission with information about violations of the federal

securities laws.³⁷ Previously, the SEC could provide awards for information relating to insider trading only. Now, the SEC can make payments regarding any securities law action that results in a civil penalty or disgorgement.³⁸

One question that arises under these new whistleblower provisions is whether potential whistleblowers now will be incentivized to report to the SEC on matters relating to Dodd-Frank Section 954 clawbacks. If the SEC enforces Section 954 aggressively so that issuers must literally seek clawbacks after *any* restatement, no matter how small and even restatements that do not result from misconduct, but reflect simply innocent accounting errors, great uncertainty over compensation may lie ahead both for companies and their senior executives.³⁹

Potential for Strict Liability Enforcement in the Banking Industry

The banking industry is another area in which there is the potential for increased enforcement activity against executives regardless of fault. Recently, the FDIC announced that it has undertaken criminal investigations aimed at 50 executives and directors of U.S. banks that have collapsed during the financial crisis.⁴⁰ These criminal investigations are separate from the civil enforcement actions contemplated by the FDIC to recover more than \$2 billion in compensation from officers of failed banks. Thus far, the FDIC has approved the filing of civil lawsuits against more than 80 officers and directors of failed banks. Richard Osterman, acting general counsel at the FDIC, recently said in an interview: "These numbers will continue to increase as time goes on."⁴¹

The civil cases the FDIC has filed to date are premised on traditional fault-based theories. One suit, filed against four former executives of IndyMac Bancorp.,⁴² seeks \$300 million in damages from the former executives based upon their alleged negligence and breach of fiduciary duties in connection with, among other things, negligently

approving and renewing loans.⁴³ A second suit, filed against eleven former directors and officers of the failed Heritage Community bank, seeks at least \$20 million⁴⁴ based on allegations that the defendants engaged in negligence, gross negligence, and breach of fiduciary duty by, among other things, failing to properly manage and supervise Heritage's commercial real estate lending program.

However, the FDIC does have authority to hold bank directors personally liable for failing to properly implement or oversee the internal controls of a banking organization.⁴⁵ At least one case, *In the Matter of Cornerstone Community Bank*, indicates that the FDIC may do so *even in the absence of knowledge or bad faith on the part of the bank director*.⁴⁶ In *Cornerstone*, the FDIC assessed a "First-Tier" monetary penalty on an outside director of Cornerstone Community Bank, who sat on the audit committee.⁴⁷ An Administrative Law Judge (ALJ) determined that the bank had violated Sections 23A and 23B of the Federal Reserve Act by extending credit to its holding companies.⁴⁸ The ALJ accepted the outside director's claim that she was not aware of the violation before learning of it from the FDIC, and that she could not have prevented it as an outside director.⁴⁹ Nevertheless, the ALJ, and subsequently the FDIC, upheld the assessment of the penalty, reasoning that a first-tier penalty may be assessed on a showing of a violation of the law, without a showing of knowledge or intent on the part of the director:

A fundamental duty of a bank board of directors is 'to monitor operations to ensure that they are controlled adequately and are in compliance with laws and policies' . . . A director cannot ignore this duty even after warnings and expect her inattention to protect her from First Tier penalties when regulatory violations flourish because of her laxity.⁵⁰

The FDIC has not yet used this authority in connection with the most recent banking crisis, but

the potential exists as part of an increase in enforcement actions in the banking industry.

What Should Corporate Executives Do in Light of These Enforcement Trends?

More than ever, corporate executives must be vigilant to ensure that their compliance programs and internal controls are effective. Although the remedies discussed above can be sought without regard to individual fault, the government tends to reserve its enforcement powers for cases involving clearly wrongful conduct. The ability to defend a commitment to compliance may be determinative in persuading government officials not to exercise the sweeping powers available to them. Therefore, corporate executives should make sure their vigilance can be documented after the fact, in the event an investigation arises. This may not preclude liability under the *Park* doctrine, or even under Sarbanes-Oxley Section 304, but as a practical matter both the SEC and DOJ may be influenced, in the exercise of their discretion over charging decisions, by a record which demonstrates serious compliance efforts.

More importantly, a strong commitment to ethics and compliance can maximize the likelihood that potential problems will be identified promptly and corrected, before they lead to costly and disruptive governmental investigations. Although a lengthy discussion of how to implement an effective compliance program is beyond the scope of this article, management should ensure that, at a minimum, corporate compliance efforts meet the standards set out in the United States Sentencing Guidelines.⁵¹ These standards, entitled “Effective Compliance and Ethics Programs,” were revised most recently in November 2004, and therefore the government will have little patience for a corporation or its officers who have failed to enact programs meeting these requirements.⁵²

Finally, compliance officers, and senior officials contemplating improvements in compliance, should pay particular attention to the decision-making

process involved in their programs for reporting potential violations. It is critical that an internal reporting process move quickly enough to permit the organization to make prompt decisions about whether to disclose an issue to the government. In some situations, such as the discovery of a material accounting error requiring a revenue restatement, disclosure may be required, while in other cases, self-reporting may be discretionary. Timely disclosure to the government may become a determining factor for avoiding enforcement efforts.

While it remains to be seen exactly how the government will use the tools in its arsenal to increase enforcement against corporate executives, a strong commitment to compliance is the best approach to minimize risk both to the organization and its management.

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¹ *Scales v. United States*, 367 U.S. 203, 224-25 (1961).

² O.W. Holmes, *The Common Law*, 50 (1881).

³ 421 U.S. 658, 673 (1975).

⁴ *Id.*

⁵ See, e.g., *United States v. New Eng. Grocers Supply Co.*, 488 F. Supp. 230, 234 (D. Mass. 1980); *United States v. Park*, 421 U.S. 658, 673 (1975).

⁶ For examples of cases in which the impossibility defense has failed, see *United States v. Gel Spice Co.*, 773 F.2d 427 (2d Cir. 1985); *United States v. Y. Hata & Co.*, 535 F.2d 508, 515 (9th Cir. 1976).

⁷ See Plea Agreements entered into by Michael Friedman, President and CEO; Howard R. Udell, Executive Vice President and Chief Legal Officer; and Paul Goldenheim, M.D., formerly Executive Vice President, Chief Scientific Officer and head of research and development in *United States v. The Purdue Frederick Co. Inc. et. al.*, Case No. 1:07CR00029 (W.D.Va. 2007).

⁸ *United States v. Sally Miller, Stephen Miller and ChemNutra Inc.*, Case No. 08-00023-01CR (W.D. Mo. 2009).

⁹ See *id.* (Transcript of Sentencing Proceeding Before The Honorable John T. Maughmer United States Magistrate Judge, dated Feb. 5, 2010).

¹⁰ DOJ Press Release, U.S. Attorney's Office for the Eastern District of Pennsylvania (June 16, 2009), available at <http://www.justice.gov/usao/pae/News/Pr/2009/jun/synthesrelease.pdf>.

¹¹ *Id.*

¹² See *Firm Guilty In Medical-Test Case*, Boston Globe, Dec. 1, 2010, available at http://www.boston.com/business/healthcare/articles/2010/12/01/firm_guilty_in_medical_test_case. On the corporate side, in November of 2010, U.S. District Judge Legrome D. Davis approved a plea agreement under which Synthes pleaded guilty to one misdemeanor count of shipping a mislabeled product, and Norian pleaded guilty to one felony count of conspiring to impede FDA functions and 110 misdemeanor counts of shipping a mislabeled product. *United States v. Norian Corporation, et al.*, Case No.; 09-403 (E.D. Pa.); see also DOJ Press Release, U.S. Attorney's Office for the Eastern District of Pennsylvania (October 4, 2010), available at http://www.justice.gov/usao/pae/News/Pr/2010/Oct/synthes,norian_release.pdf.

¹³ FDA Regulatory Procedures Manual, Ch. 6, Sec. 5-3, entitled "Special Procedures and Considerations for Park Doctrine Prosecutions" (2011).

¹⁴ *Id.* The regulations further state that "[o]ther factors to consider include but are not limited to: 1. Whether the violation involves actual or potential harm to the public; 2. Whether the violation is obvious; 3. Whether the violation reflects a pattern of illegal behavior and/or failure to heed prior warnings; 4. Whether the violation is widespread; 5. Whether the violation is serious; 6. The quality of the legal and factual support for the proposed prosecution; and 7. Whether the proposed prosecution is a prudent use of agency resources." *Id.*

¹⁵ See Duff Wilson, *Side Effects May Include Lawsuits*, N.Y. Times, Oct. 2, 2010, available at <http://www.nytimes.com/2010/10/03/business/03psych.html>.

¹⁶ Anna Edney, *Drugmaker CEOs May Be Targets for U.S. FDA in Off-Label Cases, Lawyer Says*, Bloomberg News, Oct. 14, 2010, available at [\[14/drugmaker-executives-may-become-targets-of-fda-for-off-label-promotions.html\]\(http://www.bloomberg.com/news/2010-10-14/drugmaker-executives-may-become-targets-of-fda-for-off-label-promotions.html\).](http://www.bloomberg.com/news/2010-10-</p></div><div data-bbox=)

¹⁷ See Complaint for Declaratory, Injunctive and Other Relief filed in *Friedman, et al. v. Sebelius, et al.*, Case No. 09-2028, D. D.C.

¹⁸ See Memorandum Opinion, dated December 13, 2010, filed in *Friedman, et al. v. Sebelius, et al.*, Case No. 09-2028, D. D.C.

¹⁹ *Id.* at 17 (internal quotations omitted).

²⁰ *Id.* at 18 (citing *Park*, 412 U.S. at 671).

²¹ See Section 1128 (b)(15) of the Social Security Act (42 U.S.C. § 1128(b)(15)).

²² See OIG notice entitled "Guidance for Implementing Permissive Exclusion Authority Under Section 1128(b)(15) of the Social Security Act." A copy of the notice is available on OIG's website at http://oig.hhs.gov/fraud/exclusions/files/permissive_excl_under_1128b15_10192010.pdf

²³ *Id.*

²⁴ Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (codified as amended in various sections of 15 U.S.C.) (emphasis added). Section 304(b) provides that "[t]he Commission may exempt any person from the application of [the statute], as it deems necessary and appropriate."

²⁵ See *SEC v. Jenkins*, 718 F. Supp. 2d 1070 (D. Ariz. June 9, 2010).

²⁶ *Id.* at 1074.

²⁷ *Id.* at 1077.

²⁸ *Id.*

²⁹ See *SEC v. McGuire*, C.A. No. 07-CV-4779-JMR/FLN (D. Minn. Dec. 6, 2007).

³⁰ See, e.g., *id.*; *SEC v. Jasper*, No. 07-cv-06122 HRL (N.D. Cal. Dec. 4, 2007); *SEC v. Mercury Interactive LLC et al.*, No. 07-cv-2822 (RS) (N.D. Cal. May 31, 2007).

³¹ Dodd-Frank Wall Street Reform and Consumer Protection Act, H.R. 4173, 111th Cong., at § 954(b)(2) (2010).

³² Congress does not define the term "executive officer" in Dodd-Frank, appearing to defer to the SEC to supply this definition. The SEC may consider Rule 3b-7 of the Securities Exchange Act of 1934, which provides that an "executive officer" is a company's "president, any vice president . . . in charge of a principal business unit, division or function . . . or any other person who performs similar policy making functions for the registrant." Securities and Exchange Act of 1934, 17 C.F.R. § 240.3b-7 (1991). The SEC also could adopt a new definition for the term "executive officer" in the context of Dodd-Frank.

³³ Dodd-Frank, H.R. 4173, 111th Cong., at § 954(a) (2010).

³⁴ See Implementing the Dodd-Frank Wall Street Reform and Consumer Protection Act, *available at* <http://www.sec.gov/spotlight/dodd-frank.shtml> (SEC to propose rules regarding recovery of executive compensation in August-December 2011).

³⁵ Press Release, Securities & Exchange Commission, SEC Proposes New Whistleblower Program Under Dodd-Frank Act (Nov. 15, 2010) *available at* <http://www.sec.gov/news/press/2010/2010-213.htm>.

³⁶ *Id.* at § 21F(a)(1) (2010).

³⁷ In response to the enactment of Dodd-Frank, the SEC recently proposed rules for revising its whistleblower program. The stated purpose of the new rules is to provide a “simple, straightforward” whistleblower program “to reward individuals who provide the agency with high-quality tips that lead to successful enforcement actions.” To be considered for an award, a whistleblower must voluntarily provide the SEC with original information about a violation of the federal securities laws that leads to a successful enforcement action resulting in monetary sanctions totaling more than \$1 million.

³⁸ Dodd-Frank also creates a substantially stronger financial incentive for whistleblowers by establishing a minimum award of 10 percent of the monetary sanctions recovered, and a maximum award of 30 percent. Previous insider trading programs limited a whistleblower’s potential award to just 10 percent of the recovered amount. Additionally, monetary sums in related actions, such as criminal prosecutions, may be included in calculating an award under the new law. Also, Dodd-Frank strengthens protections afforded to whistleblowers, allowing informants who believe they have been subject to discrimination and/or retaliatory termination to bring federal actions within six years. Under the Sarbanes-Oxley Act, whistleblowers had to bring their cases before Department of Labor judges and faced a 90-day statute of limitations.

³⁹ The SEC’s new proposed whistleblower rules include some provisions designed to discourage prospective whistleblowers from “front running” internal investigations simply to receive a whistleblower award. For example, the rules would treat an employee as a whistleblower under the SEC program as of the date the employee reports the information internally, as long as the employee provides the same information to the SEC within 90 days. In addition, the rules would permit the SEC to consider higher percentage awards for whistleblowers who first report their information

through effective company compliance programs. It remains to be seen, however, how the interplay between the whistleblower rules and Dodd-Frank Section 954 will play out in practice.

⁴⁰ Jean Eaglesham, *U.S. Sets 50 Bank Probes*, Wall Street Journal (Nov. 17, 2010), *available at* <http://online.wsj.com/article/SB10001424052748703628204575619000289073686.html>; See also Marcy Gordon, *US launches criminal probes into banks*, Associated Press (Nov. 17, 2010), *available at* http://news.yahoo.com/s/ap/20101117/ap_on_bi_ge/us_fdic_bank_investigations).

⁴¹ *Id.*

⁴² *FDIC v. Van Dellen, et al.*, U.S. District Court, C.D. Cal., No. SACV 10-004915 (Jul. 2, 2010).

⁴³ *Id.*

⁴⁴ See *FDIC v. Saphir, et al.*, U.S. District Court, N.D. Ill., No. 1:10-cv-07009 (2010).

⁴⁵ See Sections 8(i) and 8(j) of the Federal Deposit Insurance Act, 12 U.S.C. § 1818(i).

⁴⁶ See *In the Matter of Cornerstone Cmty. Bank*, FDIC-00-050k (June 3, 2003 F.D.I.C.).

⁴⁷ *Id.*

⁴⁸ *Id.*

⁴⁹ *Id.* at *16-17 (internal citations omitted).

⁵⁰ *Id.* at *17-19.

⁵¹ See U.S.S.C. Sentencing Guidelines Manual, § 8B2.1.

⁵² To be deemed to have an effective compliance program, the Guidelines require that corporations exercise due diligence to prevent and detect criminal conduct and otherwise promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law. The Guidelines lay out the following specific minimum requirements: (1) the organization must establish standards and procedures to prevent and detect criminal conduct; (2) top management must have effective knowledge and oversight of the compliance program and appropriately delegate responsibility for compliance; (3) the organization should use diligence to ensure that individuals with substantial authority within the organization have not engaged in illegal activities or activities inconsistent with an effective compliance program; (4) the organization must have effective compliance training; (5) the organization must ensure that compliance is monitored, and audited and that effective systems exist for reporting potential or actual criminal conduct; (6) the compliance program must be enforced and include appropriate disciplinary measures; and (7) if criminal conduct is detected, the organization

must take responsible steps to respond appropriately to the criminal conduct and to prevent further similar conduct. See U.S.S.C. Sentencing Guidelines Manual, § 8B2.1.