TOPIC 4
CORPORATE CIVIL AND ADMINISTRATIVE ENFORCEMENT POLICY

Introductory Note: This Topic sets forth policies to guide civil and regulatory enforcement authorities in developing policies to govern their enforcement officials' determinations; in determining which, if any, form of nontrial resolution and collateral consequences are appropriate for an organization that committed knowing or intentional material corporate misconduct. These policies focus on the choice of nontrial resolution in circumstances in which a determination that the organization is culpable for the misconduct, or the imposition of particular remedies, could trigger the presumptive or mandatory imposition of collateral consequences, such as debarment, exclusion, or delicensing, in the United States or abroad. This Topic also addresses enforcement officials' actions to protect employees who report misconduct internally or to government authorities from either contractual provisions that deter such reporting or from retaliatory actions. While the Sections in this Topic do not expressly apply to nontrial resolutions predicated on either negligence or strict liability, civil or regulatory authorities may find that these Sections offer guidance in such circumstances, depending on the nature of the harm, the statutory violation, and the organization's legal-reporting obligations.

In setting forth policies guiding the use of different forms of nontrial resolution, the Sections in this Topic distinguish between forms of resolution based on the legal effect the resolution would have on an organization, instead of based on the form of the resolution itself (e.g., deferred prosecution agreement, consent decree, or injunction). This Topic focuses on the consequences of the nontrial resolution, rather than developing policies for specific legal forms of nontrial resolution, because policies governing enforcement should be predicated on the consequences of the enforcement action. Across the different agencies and industries, each specific type of civil and administrative nontrial resolution can have materially different consequences for an organization depending the legal violation, the industry in which the organization operates, and the enforcement authority responsible for the resolution. Thus, in order to focus on the consequences that should guide enforcement decisions, these Sections predicate the guidance on the consequences of a nontrial resolution for knowing or intentional misconduct rather than on specific forms of nontrial resolution. Specifically, these Sections focus on three questions. First, when should civil or administrative enforcement officials employ, or agree to not employ, a nontrial resolution that could trigger mandatory, presumptive, or permissive collateral

consequences? Second, when should civil or administrative enforcement officials allow an organization to enter into a nontrial resolution that does not require the organization to admit that it engaged in the misconduct? Finally, when should civil or administrative enforcement officials allow an organization to enter into a resolution that allows the organization not to admit to the misconduct while also prohibiting it from denying that it engaged in the misconduct? It is important to develop policies governing decisions affecting these three consequences of a nontrial resolution because these consequences are material to the public and also will directly affect organization's incentives to self-report and fully cooperate.

These Sections assume that organizations' civil and administrative liability is governed by respondeat superior, as is generally the case under state and federal law. They also apply to enforcement under other organizational liability rules.

§ 6.21. Forms of Civil Nontrial Resolutions and Sanctions for Organizations

(a) Civil and regulatory enforcement officials may resolve a matter with an organization that they have determined engaged in knowing or intentional material misconduct through the following forms of nontrial resolutions:

(1) a resolution in which the organization is formally adjudicated without a trial to have committed the misconduct;

(2) a full-admission resolution under which the organization is required to admit to all of the facts needed to establish that the organization engaged in the misconduct but is not formally adjudicated to have committed the misconduct (e.g., many regulatory deferred prosecution agreements);

(3) a partial-admission resolution under which the organization admits to some of the material facts of the misconduct, but not to all the facts needed to establish that it engaged in the misconduct, and is not formally adjudicated to have committed the misconduct;

(4) a neither-admit-nor-deny resolution under which the organization is found to have engaged in the misconduct and is prohibited from publicly denying that it engaged in the misconduct (except in certain limited circumstances, such as in litigation against the organization by a party other than the enforcement authority

that entered into the resolution), but is not required to admit that it engaged in misconduct; or

(5) a no-admission/denial-permitted resolution under which the organization is found to have engaged in the misconduct, but is not required to admit to any facts of the misconduct and may publicly deny that it engaged in the misconduct.

(b) Civil and regulatory authorities may seek a variety of forms of relief including:

(1) civil or administrative monetary sanctions;

(2) an injunction against future misconduct;

(3) disgorgement or forfeiture of the benefit of misconduct;

(4) remediation;

(5) restitution;

(6) debarment, exclusion, or delicensing; and

(7) remedial measures, such as requiring compliance-program reforms and appointing a compliance monitor.

Comment:

a. Mandatory or presumptive collateral consequences of civil or administrative resolutions. The selection of the form of nontrial resolution and the form of relief can have material implications for whether an organization is subject to mandatory, presumptive, or permissive collateral consequences. A variety of statutes provide that if an organization is subject to specific forms of civil or administrative resolution, a regulatory authority can—and in some cases must—impose collateral consequences such as delicensing of the organization by federal, state, local, or foreign government agencies or debarment or exclusion of the organization from contracting with or providing services to such agencies or customers whose costs are covered by such agencies. Organizations' basis for concern about collateral consequences extends beyond those that can be imposed by government authorities. In addition, in some circumstances, self-regulatory organizations, or international organizations such as the World Bank or International Monetary Fund, that serve as gatekeepers for certain markets or sources of financing also can impose collateral consequences on an organization with detected misconduct. Private contracts also can include clauses that subject an organization adjudicated to have committed specific offenses to collateral consequences.

The collateral consequences of a civil or administrative resolution does not depend entirely or even primarily on the form of the nontrial resolution. Instead it can depend on what enforcement authority brought the action, what organization is the subject of the action, the type of misconduct, and the sanctions imposed. For example, in some circumstances, an organization can be found culpable for engaging in material misconduct without that finding triggering mandatory, presumptive, or permissive collateral consequences imposed by government authorities, self-regulatory authorities, or international organizations in the United States or abroad. In other circumstances, mandatory, presumptive, or permissive collateral consequences are triggered if an enforcement authority enters into a resolution that results in a formal adjudication that an organization engaged in misconduct, but they are not triggered if the enforcement authority enters into a resolution that does not result in a formal adjudication that the organization is culpable. Yet there are other situations in which an organization is potentially subject to collateral consequences even if it enters into a resolution that does not require it to admit culpability. For example, a no-admission resolution that is predicated on a regulatory authority's factual finding that an organization engaged in a particular form of misconduct can serves as the trigger for that regulatory authority or another entity, such as a self-regulatory organization, to impose collateral consequences on . For this reason, the Sections in this Topic are predicated on whether a nontrial resolution could trigger mandatory, permissive, or presumptive collateral consequences and not on the specific form of nontrial resolution imposed.

Some statutes allow a governmental regulatory authority to waive imposing collateral consequences at its discretion. Others limit its ability to waive. Some government authorities determine whether to impose collateral consequences at the same time they enter into a resolution with an organization. Others authorities make the decision whether to impose collateral consequences separate from its decision as to what form on nontrial resolution to use.

When enforcement of a statute or regulation could result in a civil or administrative enforcement action that triggers mandatory, presumptive, or permissive collateral consequences imposed by governmental authorities, self-regulatory authorities, or international organizations, government authorities should ensure that civil and administrative enforcement officials are able to enter into forms of nontrial resolution for corporate misconduct that do not result in such collateral consequences, to the extent they have legal authority to do so. Civil and regulatory

authorities also should provide guidance on when it is appropriate for civil or administrative enforcement officials to do so.

This Section provide guidelines on enforcement policies to guide the use of forms of nontrial resolution that avoid triggering collateral consequences that would otherwise result from enforcement of the misconduct in question. The guidelines do not specify the specific form of resolution that should be adopted because different forms of nontrial resolution and different remedies may or may not trigger collateral consequences depending on the industry, the regulatory authority, and the type of misconduct. See § 6.24, Comment *b*.

b. Civil or administrative settlement that adjudicates that an organization engaged in misconduct. Civil enforcement authorities can file a civil action in court, and administrative enforcement authorities can bring an administrative action before the relevant administrative agency, and then simultaneously or subsequently enter into a settlement with the organization under which the organization accepts certain findings of facts, conclusions of law, or determinations of liability with respect to the misconduct at issue and agrees to the remedies set forth in the settlement. Section 6.21(a) describes the various forms such a settlement may take. Section 6.21(b) lists possible remedies that a settlement can provide. These remedies can include monetary penalties, disgorgement, restitution, remediation of the harm caused, an injunction against future misconduct, and internal reforms.

Some settlements filed in court can result in a formal legal determination that the organization committed the misconduct. Agencies entering into settlements also can, and regularly do, make a legal determination, based on evidence, that the organization committed the misconduct. An organization that has thus been adjudicated to have engaged in misconduct, that admits to having engaged in misconduct, or is subject to particular forms of relief as a result of a determination that it engaged in certain types of misconduct may be subject to mandatory, presumptive, or permissive collateral consequences, as is discussed in Comment *a*. Section 6.24 provides guidance on when enforcement officials should offer to resolve a civil or administrative enforcement action through a form of nontrial resolution that would not trigger mandatory, presumptive, or permissive collateral consequences that otherwise might follow from an enforcement action.

A determination that an organization engaged in misconduct, or an organization's admission either to having engaged in misconduct or to facts that constitute misconduct, also can

have material effects on both the public and the organization that go beyond any potential collateral consequences. The public potentially benefits because such determinations provides it—and thus potential customers, employees, creditors, and suppliers—with credible evidence about whether the organization engaged in the misconduct. The organization can incur costs beyond any potential collateral consequences because such determinations can be introduced against the organization in other actions—enforcement actions, criminal actions, and private civil litigation—to establish that the organization engaged in misconduct. Section 6.25 provides guidance on when enforcement officials should require a determination of culpability or a full admission by the organization and when, by contrast, enforcement officials should offer to resolve a matter through a nontrial resolution that does not adjudicate the organization's culpability.

c. Nontrial resolutions with admissions of facts but no legal determination of culpability: Nontrial resolutions of civil or administrative actions can require an organization to admit to all, or some, of the facts of the misconduct and impose sanctions for the misconduct, without also providing a legal determination that the organization committed the misconduct. A nontrial resolution with admissions can provide the public with material information about whether the organization engaged in misconduct, although the public may view it as less credible than a litigated determination that the organization engaged in misconduct. An organization that admits to all the facts of the misconduct may incur costs to the extent that other government authorities, self-regulatory agencies, or private parties can introduce the admission in separate actions as evidence to establish the organization's culpability.

Nontrial resolutions that do not adjudicate the organization's culpability but do require it to admit to the facts of the misconduct can take a variety of forms. Two forms that arose in the criminal context but are now being used by some civil or administrative enforcement authorities are deferred prosecution agreements (DPAs) and non-prosecution agreements (NPAs). Under a civil or administrative DPA, the enforcement authority files a complaint against the company but suspends the action as long as the company complies with the provisions in the DPA. Under a civil or administrative NPA, the civil or regulatory enforcement authority agrees not to file an action against the company, provided that the company complies with the provisions in the NPA.

Civil DPAs and NPAs can impose the same financial penalties and the same non-financial consequences (such as mandated internal reforms, appointment of a compliance monitor, or an obligation to report to criminal or civil authorities) as would be imposed on an organization after

a successful trial in a civil or administrative enforcement action. The primary impact of resolving a civil or administrative case through a DPA or NPA, instead of a formal enforcement action, is that a DPA or NPA does not result in a formal legal determination that the organization committed the misconduct. By contrast, a settlement in which the organization is adjudicated to be culpable of the misconduct by a court or agency often can trigger mandatory or presumptive collateral consequences and also establish the organization's liability for purposes of a private action by civil litigants.

There is a central distinction between civil DPAs and neither-admit-nor-deny resolutions and other consent decrees. DPAs include both a statement of facts and an admission by the organization that it engaged in the facts that constitute the misconduct. By comparison, neither-admit-nor-deny resolutions, and many consent decrees, tend to involve a court's or administrative agency's factual finding that an organization engaged in misconduct, but they do not require the organization to either admit that it engaged in the misconduct or make factual admissions relating to the misconduct.

Organizations that enter into consent decrees usually are not required to either admit culpability for the misconduct or to the facts of the misconduct. In some situations, however, this distinction is less material that it would appear. While a neither-admit-nor-deny resolution does not entail an admission by the organization, it may follow a factual finding by a regulator, such as the Securities and Exchange Commission, that the organization engaged in misconduct. The finding, in turn, could trigger the mandatory, presumptive, or permissive imposition of collateral consequences. Some regulated organizations also are potentially subject to collateral consequences if they were enjoined from violating certain statutes, regardless of whether the organization admitted culpability.

In the criminal context, DPAs tend to require organizations to admit of all the facts of the misconduct. Civil and administrative DPAs should require admissions of facts of the misconduct (the act) to the extent this can be done in accordance with the principles in this Section. In accordance with § 6.24, enforcement officials should allow organizations that self-report or fully cooperate to admit to most of the facts of the misconduct without admitting to every fact (e.g., scienter) needed to establish the organization's legal liability for the misconduct.

Civil and regulatory enforcement authorities should enable their enforcement officials to employ DPAs and NPAs, consistent with this Section, if: (1) the enforcement authority is able to

use DPAs and NPAs; and (2) the enforcement authorities' jurisdiction includes situations in which a successful formal enforcement action could trigger mandatory, presumptive, or permissive collateral consequences (see Comment *a*).

d. Nontrial resolutions without admissions: Consent decrees. Consent decrees are a regularly-used form of nontrial resolution. Under a negotiated consent decree, an organization agrees to comply with the order's remedial requirements but generally does not formally admit that it has committed a violation of the law. An organization that enters into a consent decree that that does not constitute a "neither admit nor deny" resolution is not estopped from denying that it engaged in the misconduct.

Civil and administrative enforcement authorities enter into a consent decree after concluding that an organization engaged in material misconduct. Some administrative agencies entering into a consent decree do so only after making a formal finding that the organization engaged in misconduct. The administrative agency's factual findings that an organization engaged in material misconduct can serve as the basis for the agency's decision to impose collateral consequences on the organization if it has authority to do so and the organization engaged in the type of misconduct that could serve as a predicate for collateral consequences. Such a factual finding also could trigger collateral consequences imposed by others.

Consent decrees generally do not require organizations to admit to the misconduct or to the facts of the misconduct. Some consents decrees preclude an organization from denying their misconduct (except in actions brought by third parties). Others stipulate that the organizations need not admit to their misconduct but do not preclude the organizations from publicly denying that they engaged in the misconduct that was alleged.

Consent decrees are filed in court or with the relevant administrative agency. An organization must comply with the terms of a consent agreement, usually under threat of contempt sanctions for failure to do so.

Consent decrees should contain the following elements:

(1) a description of the facts of the misconduct that the organization engaged in;

(2) a statement of any remedial actions and other internal reforms that the organization has undertaken voluntarily;

(3) an agreement by the organization to cooperate with any ongoing investigation of the misconduct by the civil or administrative enforcement authority that brought the enforcement action;

(4) provisions that govern the monetary sanctions, disgorgement, or other remedial measures (such as internal reforms) imposed by the nontrial resolution;

(5) a reporting requirement under which the organization must provide periodic reporting to the civil or administrative enforcement authority with jurisdiction over the action regarding its compliance with the consent decree; and

(6) a provision that delineates the specific and measurable actions that would trigger the termination of the consent decree, as well as a provision that specifies the date on which the agreement terminates, regardless of the decree's specific requirements. If a monitor is imposed, the agreement should include provisions relating to the appropriate scope, selection, and governance of the monitor, in accordance with §§ 6.10–6.12.

e. Nontrial resolutions without admissions: neither-admit-nor-deny resolutions. Neither-admit-nor-deny resolutions are nontrial civil or administrative resolutions under which an organization is subject to remedial measures for its misconduct and is not allowed to deny that it engaged in the misconduct (except in litigation brought by other enforcement authorities or private litigants), but is not required to admit that it engaged in the misconduct.

Neither-admit-nor-deny resolutions often take the form of an administrative resolution entered into by an administrative enforcement authority after it has concluded that an organization engaged in material misconduct. The resolution does not require the organization to admit that it engaged in the misconduct, but it does preclude the organization from denying that it engaged in the misconduct, except to defend itself in actions brought against it by other enforcement authorities or by private litigants.

Administrative enforcement authorities enter into neither-admit-nor-deny resolutions after concluding that an organization engaged in material misconduct. Some agencies make formal findings that organizations engaged in misconduct. An agency's factual findings that an organization engaged in material misconduct can serve as the basis for the agency's decision to impose collateral consequences on the organization if it has authority to do so and the organization engaged in the type of misconduct that could serve as a predicate for collateral consequences.

Neither-admit-nor-deny resolutions usually should contain the following elements:

(1) a description of the facts of the misconduct that the organization engaged in;

(2) a statement that the organization cannot deny that it engaged in misconduct, except in litigation brought by other enforcement authorities or private litigants;

(3) a statement that the organization does not admit that it engaged in misconduct;

(4) an agreement by the organization to cooperate with any ongoing investigation by the government of the misconduct;

(5) a statement of any remedial actions that the organization has agreed to undertake;

(6) provisions that govern the remedies imposed;

(7) a reporting requirement under which the organization must provide periodic reporting to the enforcement authority with jurisdiction over the enforcement action regarding its compliance or noncompliance with the resolution; and

(8) a provision that states the specific and measureable actions that would trigger the termination of the resolution, as well as a provision that specifies the date on which the resolution terminates, regardless of its specific requirements.

f. Cease-and-desist orders. An administrative agency may have authority to impose a cease-and-desist order. A cease-and-desist order enjoins an organization from future violations of the law. It also can impose monetary penalties and remedial measures.

This Section provides guidance on when it is appropriate to structure cease-and-desist orders to avoid either adjudicating an organization’s culpability or requiring it to admit to the full facts of certain forms of misconduct, when it is possible to do so. They also bear on when other forms of resolution should be employed in situations in which it is not possible to structure a cease-and-desist order to avoid either triggering mandatory, presumptive, or permissive collateral consequences or establishing facts that would determine the organization’s liability in an action brought by third parties.A cease-and-desist order is predicated on a legal finding, for example, by an administrative agency, that the organization engaged in misconduct. The nontrial resolution imposing the order can be structured so that the organization does not admit that it engaged in the misconduct. A cease-and-desist order may, but does not have to, include a clause that precludes the organization from denying that it engaged in the misconduct. The organization must comply with the terms of the cease-and-desist order under threat of contempt sanctions for failure to do so.

A cease-and-desist order should contain the following elements:

(1) a finding of fact regarding and description of the facts of the misconduct that the organization engaged in;

(2) an order requiring the organization not to commit future violations of the laws at issue;

(3) a statement of any remedial actions that the organization must undertake;

(4) a requirement that the organization shall cooperate with any ongoing investigation into the misconduct by the enforcement officials with jurisdiction over the cease-and-desist order;

(5) provisions governing the remedies imposed;

(6) a reporting requirement under which the organization must provide periodic reporting to the enforcement authority and the court or agency with jurisdiction over the enforcement action regarding its compliance or noncompliance with the cease-and-desist order; and

(7) a provision that states the specific and measurable actions that would trigger the termination of the cease-and-desist order, as well as a provision that specifies the date that the order terminates, regardless of its specific requirements.

If a compliance monitor is imposed, the order should include provisions relating to how the monitor is selected, and the scope and governance of the monitor's authority, in accordance with §§ 6.10–6.12.

g. Injunctions. Enforcement authorities often have authority to seek an injunction. To obtain an injunction, the enforcement authority must establish a threat of future misconduct. An organization that violates an injunction can be subject to contempt sanctions. Injunctions for certain violations can result in collateral consequences. Accordingly, the guidance in this Topic applies to the use of injunctions that could trigger collateral consequences—or could provide an adjudication of culpability or an admission by the organization to the facts of the misconduct—that others could use in an action against the organization as evidence that the organization engaged in misconduct.

h. Restitution, remediation, and disgorgement. For a discussion of organizational disgorgement, restitution, and remediation, see § 6.07.

i. Collateral consequences: Debarment, exclusion, and delicensing. Principles governing the decision whether to impose collateral consequences are discussed in § 6.24, Comment *i*, and § 6.26.

REPORTERS' NOTES

a. Existing regulatory approaches. Civil and regulatory enforcement authorities have a variety of nontrial resolutions available to them. Some have officially adopted the use of deferred prosecution agreements (DPAs) and non-prosecution agreements (NPAs). The resolutions are referred to as DPAs and NPAs, notwithstanding the fact that no criminal "prosecution" is or could be contemplated. See, e.g., DIV. OF ENFORCEMENT, SEC. & EXCH. COMM'N, ENFORCEMENT MANUAL § 6.2.3. (2012), https://www.sec.gov/divisions/enforce/enforcementmanual.pdf; DEPT. OF JUSTICE; ENF'T DIV., SEC. & EXCH. COMM'N, FCPA: A RESOURCE GUIDE TO THE U.S. FOREIGN CORRUPT PRACTICES ACT 78-79 (2020) (discussing the SEC's policy on and use of DPAs and NPAs in Foreign Corrupt Practices Act cases); James McDonald, Dir., Div. of Enf't, Commodity Futures Trading Comm'n, *Perspectives on Enforcement: Self-Reporting and Cooperation at the CFTC*, COMPLIANCE AND ENFORCEMENT, https://wp.nyu.edu/compliance_enforcement 2017/09/25/; Andrew Ceresney, Dir., Div. of Enf't, Sec. & Exch. Comm'n, ACI's 32nd FCPA Conference Keynote Address (Nov. 17, 2015), https://www.sec.gov/news/speech/ceresney-fcpa-keynote-11-17-15.html (predicating DPAs and NPAs on whether the organization self-reported); see also Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act and Commission Statement on the Relationship of Cooperation to Agency Enforcement Decisions, SEC Release No. 1470, 2001 WL 1301408 (Oct. 23, 2001), https://www.sec.gov/litigation/investreport/34-44969.htm.

b. Impact on collateral consequences of DPAs, NPAs, and nontrial resolutions without admissions. A determination in court or by an administrative agency—whether following trial or through settlement of a civil or administrative action—that an organization is liable for engaging in certain types of misconduct, such as securities fraud or healthcare fraud, can result in the organization being subject to mandatory, presumptive, or permissive collateral consequences such as exclusion from doing business with a specific federal agency, debarment, or delicensing (see Comment *a*). By contrast, resolution of an enforcement action through a DPA, NPA, neither-admit-nor-deny settlement, or a consent decrees may not trigger these collateral consequences.

Even when such resolutions do not trigger collateral consequences, they do not preclude any relevant federal agency from instituting its own action to determine whether the organization or an organizational actor engaged in the misconduct and should be subject to collateral consequences, as is discussed in § 6.15, Reporters' Note *b*. For a discussion of the appropriate use of DPAs with individuals in cases in which "neither justice nor public safety demands that the individual be stigmatized by formal charge and conviction, with their attendant collateral consequences," see Model Penal Code § 6.02A, Comment *d* (AM. L. INST. 1985).

c. Impact on reputational damage to the organization of DPAs, NPAs, and nontrial resolutions without admissions. For a discussion of why publicly disclosed resolutions, such as DPAs and NPAs, that contain a statement of facts about the misconduct and require organizations to admit culpability for the misconduct are unlikely to reduce the reputational damage to the organization relative to a formal imposition of civil liability, see § 6.15, Reporters' Note *d*. This same conclusion would not apply if a resolution either is not publicly disclosed or does not require the organization to admit that it engaged in the misconduct, such as a consent decree or a neither-admit-nor-deny resolution. A person contemplating dealing with the organization (a counterparty) who is aware of such a resolution would probably be more uncertain about the organization's culpability for the misconduct following a nontrial resolution that does not require the organization to admit its misconduct than following a nontrial resolution in which the organization admits culpability.

d. Role of judges in overseeing DPAs and NPAs. For a discussion of judicial review of DPAs in the criminal context, see § 6.02, Reporters' Note l; § 6.09, Reporters' Note *a*; and § 6.12, Reporters' Note *c*.

e. Role of judges in overseeing negotiated administrative settlements, such as consent decrees. Administrative agencies have a duty to consider settlement offers, see Administrative Procedure Act (APA), 5 U.S.C. § 554(c)(1), but the APA grants considerable discretion to agencies to accept or reject an offer. Courts have consistently held that judicial review over an agency's decision to settle a pending case is narrow or nonexistent, see, e.g., Nat'l Lab. Rel. Bd. v. United Food & Com. Workers Loc. 23, 484 U.S. 112 (1987).

Courts have also held that judges have limited authority to challenge a consent decree, even when they are asked to approve the judgment. In *Sec. & Exch. Comm'n v. Citigroup Global Markets, Inc.*, the Securities and Exchange Commission (SEC) filed a complaint against Citigroup alleging, among other things, that it negligently misrepresented its role and economic interest in a billion dollar fund, in violation of Sections 17(a)(2) and (3) of the Securities Act of 1933. Shortly thereafter, the SEC proposed a consent decree which, among other things, imposed a $95 million penalty but did not require Citigroup to admit to the misconduct in the U.S. District Court for the Southern District of New York. U.S. District Judge Jed Rakoff refused to approve the consent decree and instead set a trial date. He wrote that before a court may employ its injunctive and contempt powers in support of an administrative order:

> it is required, even after giving substantial deference to the views of the administrative agency, to be satisfied that it is not being used as a tool to enforce an agreement that is unfair, unreasonable, inadequate, or in contravention of the public interest.

Sec. & Exch. Comm'n v. Citigroup Global Markets Inc., 827 F.Supp.2d 328, 334 (S.D.N.Y. 2011)

Judge Rakoff concluded that the proposed consent decree was not fair, reasonable, adequate, or in the public interest because:

> it does not provide the Court with a sufficient evidentiary basis to know whether

> the requested relief is justified under any of these standards. Purely private parties can settle a case without ever agreeing on the facts, for all that is required is that a plaintiff dismiss his complaint. But when a public agency asks a court to become its partner in enforcement by imposing wide-ranging injunctive remedies on a defendant, enforced by the formidable judicial power of contempt, the court, and the public, need some knowledge of what the underlying facts are: for otherwise, the court becomes a mere handmaiden to a settlement privately negotiated on the basis of unknown facts, while the public is deprived of ever knowing the truth in a matter of obvious public importance.

Id. (footnotes omitted).

Both the SEC and Citigroup appealed. The U.S. Court of Appeals for the Second Circuit reversed. The court concluded that a district court has authority to review a consent decree to determine whether it is "fair and reasonable" in that the public interest would not be disserved, but the court does not have authority to reject a consent decree on the grounds that it is inadequate. It also concluded that "[a]bsent a substantial basis in the record for concluding that the consent decree does not meet these requirements, the district court is required to enter the order." Sec. & Exch. Comm'n v. Citigroup Global Markets, Inc., 752 F.3d 285 (2014).

The Second Circuit went on to explain that:

> A court evaluating a proposed S.E.C. consent decree for fairness and reasonableness should, at a minimum, assess (1) the basic legality of the decree, … (2) whether the terms of the decree, including its enforcement mechanism, are clear, … (3) whether the consent decree reflects a resolution of the actual claims in the complaint … and (4) whether the consent decree is tainted by improper collusion or corruption of some kind. … The primary focus of the court's inquiry should … be on whether the consent decree is procedurally proper, using objective measures similar to the factors set out above, taking care not to infringe on the S.E.C.'s discretionary authority to settle on a particular set of terms.

The Second Circuit added that "when the proposed relief includes injunctive relief, the district court must also consider the public interest in deciding whether to grant the injunction. Id. (citations omitted).

The court concluded that it is "an abuse of discretion to require, as the district court did here, that the S.E.C. establish the "truth" of the allegations against a settling party as a condition for approving the consent decrees. Id.

f. Informal agency actions. Agencies have at times resolved matters through informal means, including threatening to take action unless an organization, or all organizations in an industry, voluntarily undertake certain reforms. Informal agency actions designed to effect industry-wide reforms should be avoided as they are not subject to either the notice-and-comment constraints associated with agency rulemaking or the valuable constraint on unfettered agency discretion that comes with judicial oversight in civil litigation. These informal actions are outside

the scope of this Section. For a discussion of the rule of law issues raised by informal agency actions see, e.g., Edward Rubin, *Executive Action: Its History, its Dilemmas, and its Potential Remedies,* 8 J. LEGAL ANALYSIS 1 (2016); Jennifer Arlen, *Prosecuting Beyond the Rule of Law: Corporate Mandates Imposed through Deferred Prosecution Agreements*, 8 J. LEGAL ANALYSIS 191 (2016); Zachary S. Price, *Seeking Baselines for Negative Authority: Constitutional and Rule-of-Law Arguments over Nonenforcement and* Waiver, 8 J. LEGAL ANALYSIS 191 (2016); see also Daniel Richman, *Federal Criminal Law, Congressional Delegation, and Enforcement Discretion*, 46 UCLA L. REV. 757 (1999); cf. KENNETH CULP DAVIS, DISCRETIONARY JUSTICE: A PRELIMINARY INQUIRY (1977); Edward Rubin, *Discretion and its Discontents*, 72 CHIC.-KENT L. REV. 1299 (1997).

Agencies also have resolved matters through arbitration and mediation. Congress authorized such forms of resolution in the Administrative Dispute Resolution Act, 5 U.S.C. § 571 et seq.

g. SEC injunctions. The SEC has authority to sue for an injunction prohibiting an organization from violating the securities laws, see, e.g., Securities Act of 1933, § 20(b), 15 U.S.C. § 78t(b); Securities and Exchange Act of 1934, § 21(d)(1), 15 U.S.C. § 78u-2(e). To obtain an injunction, courts require the SEC to establish that there exists a cognizable danger of a recurrent violation. Rondeau v. Mosinee Paper Corp., 422 U.S. 49, 59 (1975). The ultimate determination turns on whether the facts and circumstances of the defendant's past misconduct, and subsequent events, establish that there is a reasonable likelihood of future violations by the defendant. E.g., Goshen Mfg. Co. v Hubert A. Myers Mfg. Co., 242 U.S. 202 (1916); Sec. & Exch. Comm'n v. Texas Gulf Sulphur Co., 401 F.2d 833, 856-857 (2d Cir. 1968), cert. denied sub. nom. Coates v. Sec. & Exch. Comm'n, 394 U.S. 976 (1969). Misconduct that occurred many years ago and was not repeated generally will not support an injunction. The U.S. Supreme Court has described injunctions imposed for securities violations as "a drastic remedy." Aaron v. Sec. & Exch. Comm'n, 446 U.S. 680, 703 (1980).

The typical SEC injunction for fraud bars the defendant from making any future untrue statements of material fact concerning a number of specific matters, or any untrue statement of material fact similar to those statements specifically set forth in the agreement or of similar purpose and object. Sec. & Exch. Comm'n v. Savoy Indus., Inc., 665 F.2d 1310, 1316-1319 (D.C. Cir. 1981).

The SEC has authority to seek monetary penalties in any civil injunction action brought under the Securities Act of 1933, 15 U.S.C. § 77a et seq; the Securities and Exchange Act of 1934, 15 U.S.C. § 78a et seq; the Investment Company Act of 1940, 15 U.S.C. § 80a-1 et seq., and the Investment Advisors Act. Remedies Act. Pub. L. No. 101-429, 104 Stat. 931, 15 U.S.C. § 80b-1 et seq.

h. Cease and desist. In 1990, Congress authorized the SEC to issue permanent and temporary cease-and-desist orders against any respondent that the agency finds has violated or is about to violate the federal securities laws. Securities Enforcement Remedies and Penny Stock Report Act of 1990 (Remedies Act), Pub. L. No. 101-429, 104 Stat. 93 (1990) (codified as

amended in scattered sections of 15 U.S.C.). The commission can order the respondent to cease the violation, disgorge profits, and take affirmative actions to comply with the securities laws.

Other agencies, such as the Commodity Futures Trading Commission (CFTC), Federal Trade Commission (FTC), National Labor Relations Board (NLRB), and bank regulatory agencies also have cease-and-desist authority. See H.R. Rep. No. 101-616, at 23 (1990), reprinted in 1990 U.S.C.C.A.N. 1379, 1390 (same); 12 U.S.C. § 1818(b) (1994) (authorizing banking agencies to impose cease-and-desist order upon showing that person has violated law); 29 U.S.C. § 160(c) (1994) (authorizing NLRB to impose cease-and-desist order upon showing that person has violated law); 15 U.S.C. § 45(b) (1994) (authorizing FTC to impose cease-and-desist order upon showing that person has violated law); 7 U.S.C. § 13(b) (1994) (authorizing CFTC to impose cease-and-desist order upon showing that person has violated law).

An important issue with regard to cease-and-desist orders is whether a finding of a likelihood of a future violation is a prerequisite to their imposition. The SEC has concluded that to issue a cease-and-desist order it must first find some likelihood of a future violation, but the likelihood is less than is necessary for a court to issue an injunction. KPMG Peat Marwick, LLP, AAER 1360, 74 SEC Dock. 357, 380 (2001); see also Andrew M. Smith, *SEC Cease-and-Desist Orders*, 51 ADMIN. L. REV. 1197 (1999).

The CFTC requires a finding that violations are likely to persist in the future before a cease-and-desist order can be issued. See In re Brody, [1986-87 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,081, at 32,181 (May 20, 1986) (concluding that a cease-and-desist order is an appropriate enforcement tool if there is a reasonable likelihood that earlier violations will be repeated) (citing In re Dillon-Gage, Inc., [1984-86 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,574, at 30, 482-483 (June 20, 1984).

By contrast, several, but not all, courts have found that the Federal Deposit Insurance Corporation (FDIC) and other bank regulatory agencies do not need to find a likelihood of future violations prior to imposing a cease-and-desist order, in recognition of their authority to prevent unsound business practices. See Lindquist & Vennum v. Fed. Deposit Ins. Corp., 103 F.3d 1409, 1418 (8th Cir. 1997) (FDIC need only show proof of misconduct to exercise its power to order a party to cease and desist from engaging in that misconduct); Greene Cnty. Bank v. Fed. Deposit Ins. Corp., 92 F.3d 633, 636 (8th Cir. 1996) (proof of misconduct alone entitles FDIC to invoke its broad cease-and-desist enforcement powers). See, e.g., Interamericas Invs. Ltd. v. Bd. of Governors of Fed. Rsrv. Sys., 111 F.3d 376 (5th Cir. 1997); Saratoga Sav. & Loan Ass'n v. Fed. Home Loan Bank Bd., 879 F.2d 689 (9th Cir. 1989).

i. Injunctions: direct and indirect effects of a violation. An injunction compels the person or entity subject to it to obey the law upon threat of being found in contempt of the court issuing the injunction. Such a finding can result in the imposition of fines, imprisonment, or other civil or criminal penalties. Injunctions also have collateral consequences. First, an administrative injunction tends to be predicated on a finding that the organization engaged in misconduct. This finding may have a preclusive effect in subsequent litigation. Parklane Hosiery Co. v. Shore, 439 U.S. 322 (1979) (judicial findings of fact may be used offensively to establish the defendant's

misconduct in subsequent private litigation under some circumstances). In addition, an injunction may subject the organization to additional disciplinary action by the agency, including debarment, see, e.g., Exchange Act §§ 15(b)(4)(C), 15(b)(6)(A), 15 U.S.C. §§ 78o(b)(4)(C), 78o(b)(6)(A) (1994); Investment Advisers Act of 1940, §§ 3(e) and 3(f), 15 U.S.C §§ 80b-3(e), 80b-3(f) (1994 & Supp. II 1996); 15 U.S.C. §§ 78o(b)(4)(D), 78o(b)(4)(E), 78o(b)(6)(A) (1994). Certain injunctions may trigger statutory disqualification and result in loss of membership in various self-regulatory organizations, such as the securities exchanges. See Investment Company Act §§ 9(a) & 9(b), 15 U.S.C. §§ 80a-9(a), 9(b) (1994); see also Securities and Exchange Act of 1934, § 15A(g)(2) (the Financial Industry Regulatory Authority has authority to deny membership to those enjoined from violating the securities laws).

j. SEC disgorgement remedy. In Liu v. Sec. & Exch. Comm'n, 591 U.S. __, 140 S. Ct. 1936 (2020), the U.S. Supreme Court addressed the scope of the SEC's authority to seek disgorgement as a remedy in enforcement actions in federal court, as opposed to an agency administrative proceeding. The Court held that disgorgement is an appropriate and traditional equitable remedy, but placed three limitations on disgorgement. First, the remedy must be linked to each individual defendant's profits—defendants are not jointly and severally liable for the total profits gained. Second, the remedy should be based on net profits, after expenses. Finally, the remedy is justified only as a way of returning the defendant's wrongful gain to those harmed by the defendant's misconduct, although the Court left open the possibility that the government might retain the funds when it is infeasible to distribute the collected funds to investors. The Court concluded that in the case in question the SEC's pursuit of disgorgement had transgressed each of those limits. For an additional discussion of *Liu*, see § 6.07, Reporters' Note *b*.

Subsequently, Congress amended Section 21(d) of the Securities and Exchange Act of 1934 to grant the SEC express authority to obtain disgorgement in civil actions of "any unjust enrichment by the person who received such unjust enrichment as a result of such violation." The statute provides a five-year statute of limitations for most disgorgement actions, but it allows the SEC to seek disgorgement up to 10 years after the latest date of the violation for scienter-based violations, including the antifraud provisions of Section 10(b) of the Exchange Act, Section 17(a)(1) of the Securities Act, and Section 206(1) of the Investment Advisers Act. National Defense Authorization Act for Fiscal Year 2021, H.R. 6395, § 6501.

k. Enforcement actions in Article III courts vs. administrative proceedings. Federal agencies often have a choice between bringing an action for civil penalties in a district court or an administrative proceeding. Administrative proceedings are decided, initially, by administrative law judges who are employees of the agency. Some have expressed concern that administrative actions are unfair to the defendant because the agency has a "home court" advantage. See, e.g., U.S. CHAMBER OF COM. CTR. FOR CAPITAL MARKETS COMPETITIVENESS, EXAMINING U.S. SECURITIES AND EXCHANGE COMMISSION ENFORCEMENT: RECOMMENDATIONS ON CURRENT PROCESSES AND PRACTICES (July 15, 2015), http://www.centerforcapitalmarkets.com/wp-content/uploads/2015/07/021882_SEC_Reform_FIN1.pdf; see also Robert Anello, *Addressing the SEC's Administrative "Home Court" Advantage in Enforcement Proceedings*, FORBES (Sept. 7,

2015). For a defense of specialized courts see, e.g., Richard Revesz, *Specialized Courts and the Administrative Lawmaking System*, 136 UNIV. PA. L. REV. 111 (1990). One of the potential advantages of administrative enforcement is that the factual findings are made by an administrative judge with expertise in the area, instead of by a jury.

l. SEC's use of administrative actions after Dodd-Frank. The SEC enjoys particularly broad authority to pursue actions before its own administrative law judges. The Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010 authorizes the SEC to impose (in most cases) civil penalties in administrative proceedings on those violating the federal securities laws. See Stephen J. Choi and A.C. Pritchard, *The SEC's Shift to Administrative Proceedings: An Empirical Assessment*, 34 YALE J. ON REG. 1 (2017). An empirical assessment of the SEC's use of administrative actions following Dodd-Frank's enactment found that the SEC increased its use of administrative actions (both in absolute numbers and relative to civil actions). Civil penalties in both administrative and civil actions increased. Corporate cooperation also increased. The authors also found that, post-Dodd-Frank, administrative actions were less likely to prevail and less likely to garner media attention. Id. Another analysis of SEC administrative actions is: Urška Velikonja, *Are the SEC's Administrative Law Judges Biased? An Empirical Investigation*, 92 WASH. L. REV. 315 (2017).

§ 6.22. Enforcement Policy for Civil and Administrative Nontrial Resolutions

(a) A civil or administrative enforcement authority should issue and make publicly available a written enforcement policy setting forth the factors that its enforcement officials will use when determining whether to employ a form of nontrial resolution that would:

(1) trigger, or avoid triggering, mandatory, presumptive, or permissive collateral consequences;

(2) adjudicate that the organization engaged in material misconduct;

(3) require the organization to admit to all or some of the facts of the misconduct; or

(4) preclude the organization from denying—or permit the organization to deny—that it engaged in misconduct.

(b) The written enforcement policy should provide that an organization should not be granted a downward adjustment in monetary penalty based on the organization's inability to pay unless:

(1) enforcement officials have determined that the organization truly cannot pay;

(2) the organization did not make substantial disbursements to shareholders or high-level personnel during the period between when the organization became aware of the misconduct and the nontrial resolution;

(3) the organization has undertaken all appropriate remedial actions available to it, including appropriate disciplinary actions against employees and agents who committed, conspired to commit, aided and abetted the commission of the misconduct or failed to take appropriate action upon becoming aware of the misconduct, in accordance with § 6.07;

(4) the nontrial resolution is structured to place a priority on ensuring that victims receive restitution and that harm is remediated, including through measures designed to require that restitution payments be made from the organization's future earnings; and

(5) the nontrial resolution prohibits the organization from providing distributions to shareholders, or incentive compensation or bonuses to high-level personnel, until the organization has satisfied its obligations under the agreement.

Comment:

a. Policies for civil and administrative enforcement. See § 6.02 and the accompanying Comment for a discussion of the elements of an effective enforcement policy.

b. Guidance on the use of resolutions that trigger collateral consequences, adjudicate culpability, or preclude organizations from denying that they engaged in misconduct before the agency or to the public. An enforcement policy targeted at knowing or intentional material misconduct should be structured to promote deterrence, in addition to other goals of civil and administrative enforcement. Deterrence is broadly defined, in accordance with § 6.02, Comments *a* & *f*, to include any intervention designed to reduce—or induce organizations to help reduce—organizational misconduct. Enforcement authorities promote deterrence when they structure enforcement policies to provide material incentives for organizations to undertake full corrective action in accordance with § 6.01(n), as is discussed in §§ 6.02, 6.04, 6.05, 6.07 and their Comments, as well as in the Comments to §§ 6.18–6.19. As these Sections and Comments explain, organizations need material incentives to detect, investigate, and self-report misconduct; to fully cooperate (including by providing enforcement officials with evidence relating to both the full

extent of any material misconduct, as well as the role of the individuals responsible for it); and to fully remediate.

To achieve these goals, civil and administrative enforcement officials should adopt clear, written, enforcement policies that enable organizations to predict how their decisions to self-report, fully cooperate, and fully remediate will affect the form of nontrial resolution that will be offered to them. The policies also should ensure that organizations that either undertake full corrective action or fully cooperate and fully remediate will obtain resolutions that offer them predictable and substantially more favorable terms would be offered to organizations that do not undertake these actions.

Enforcement policies should therefore provide guidance relating to when enforcement authorities should use nontrial resolutions that have consequences or features that tend to be material to organizations or the public. These include the following:

(1) whether the resolution should be structured to avoid triggering mandatory, presumptive, or permissive collateral consequences imposed by federal, state, local, or foreign governmental authorities, or by self-regulatory or international organizations, that would otherwise result from a determination following a trial that the organization that engaged in the misconduct;

(2) whether the resolution should adjudicate that the organization engaged in the misconduct, or otherwise require an admission by the organization that it engaged in the misconduct, that could be used by another party (e.g., another agency or private litigants) to establish the organization's culpability for the misconduct;

(3) whether the resolution should require the organization to admit to all or some of the material facts of its misconduct;

(4) whether the resolution should preclude the organization from denying in public that it engaged in misconduct;

(5) whether the resolution should require the organization to cooperate with the enforcement authority's on-going investigation of the individuals responsible for the misconduct;

(6) whether the resolution should require the organization to undertake internal reforms or to accept a compliance monitor; and

(7) the magnitude of the penalty imposed by the nontrial resolution.

This Section focuses on providing guidance on policies relating to the first four issues. Guidance on policies for the fifth and sixth issues are governed by the principles set forth in § 6.05 and §§ 6.09–6.12.

c. Enforcement policy governing admissions and organization's ability to deny culpability. An enforcement official entering into a civil or administrative nontrial resolution often can decide whether to require the organization to admit to all, some, or none of the facts of the alleged misconduct. When the organization is not required to admit to misconduct, the enforcement official should structure the resolution to preclude the organization from denying that it engaged in the misconduct (except in litigation against it by others) or permit the organization to freely deny its culpability.

Enforcement authorities should adopt guidelines to govern—and provide organizations with notice of—the factors relevant to enforcement officials' decisions whether to offer an organization a form of nontrial resolution that requires a full or partial admission or does not require an admission at all. Enforcement authorities also should adopt and publicize policies that govern their decisions whether to permit an organization to deny its culpability in all circumstances or preclude an organization from denying that it engaged in the misconduct except in litigation brought by a third party.

In fashioning such guidelines, it is important for enforcement authorities to take into account the impact on the public—and on the effort to deter misconduct—of allowing organizations to avoid admitting and/or to deny that they engaged in misconduct. The public may have a strong interest in learning both the facts of material knowing and intentional misconduct and whether the organization had a role in the misconduct. Resolutions that allow organizations to deny legal responsibility for their misconduct are inconsistent with the goal of informing the public about the misconduct when used in cases in which enforcement officials have sufficient evidence to prove that the organization engaged in the misconduct.

A resolution that allows an organization to deny that it engaged in misconduct can also harm efforts to deter misconduct because it can signal to the organization's employees that the actions that led to the sanctioned conduct were not unlawful or unethical. By contrast, a resolution that requires an organization to admit misconduct or precludes it from denying it can promote the effectiveness of the organization's compliance function. An organization can more effectively undertake internal reforms—and send a clear message to employees that they should not engage

in the types of conduct that led to the violation—if the organization must admit that the actions for which it was held liable did indeed constitute misconduct.

Notwithstanding these concerns, there are circumstances in which enforcement authorities can best serve the public interest by allowing organizations to enter into resolutions that do not require them to admit to all of the elements of their misconduct. No-admissions resolutions should only be used with organizations whose misconduct could be proven in court if their use substantially enhanced deterrence by inducing self-reporting or full cooperation. No-admission resolutions can be structured to remove the risk to organizations of the collateral consequences that can result from other types of nontrial resolution. No-admission resolutions also can be structured so that private litigants cannot use them as evidence against the organizations. Because no-admission resolutions provide a substantial benefit to organizations, these resolutions can promote the goals of civil and administrative enforcement *only* when used with organizations that assisted enforcement authorities by undertaking full corrective action or by fully cooperating and remediating.

Enforcement officials promote the public interest when they adopt a presumption than an organization that committed knowing or intentional material misconduct can avoid admitting to all of the facts of its misconduct *only* if the admission could subject the organization to costs imposed by third parties *and* the organization actively sought to aid enforcement authorities by: (1) undertaking full corrective action, as defined in § 6.01(n); or (2) cooperating and remediating, in accordance with § 6.24(b) or in accordance with and under the circumstances set forth in § 6.24(c). If an enforcement authority can show that an organization engaged in knowing or intentional material misconduct, it should not offer a nontrial resolution that allows the organization to avoid admitting that it engaged in the misconduct in circumstances other than those specified above.

In developing a policy on partial- or no-admission resolutions, an enforcement authority should adopt a presumption that such non-trial resolutions should take the form of "no denial" resolutions in all cases of knowing or intentional material misconduct in which enforcement officials conclude that there is sufficient evidence to establish under the applicable legal standard that the organizations engaged in misconduct. A no-denial resolution precludes an organization from denying that it committed the misconduct except in litigation brought by a third party.

d. Public disclosure of civil and administrative nontrial resolutions. Nontrial civil and administrative resolutions with an organization that engaged in knowing or intentional material misconduct generally should be disclosed and made available publicly, in accordance with § 6.02(b)(5). The public disclosure should explain:

(1) the facts of the misconduct;

(2) the legal violation that the organization is alleged to have committed;

(3) the misconduct that the organization was found to have committed;

(4) the justification for using the form of nontrial resolution employed;

(5) the sanctions imposed by the resolution;

(6) any provisions for providing restitution or remediation to victims;

(7) any voluntary remediation by the organization;

(8) any required internal reforms;

(9) any appointment of a monitor;

(10) the provisions requiring the organization to report to civil or regulatory authorities its ongoing efforts to comply with the law; and

(11) the duration of the resolution.

Enforcement authorities can promote public access to their nontrial resolutions by posting them on their websites on a page dedicated to disclosure of nontrial resolutions.

Nevertheless, when an organization has engaged in full corrective action (in accordance with § 6.01(n)), then it may be appropriate for an enforcement authority to refrain from publicizing the enforcement action if doing so could subject the organization to material adverse consequences that would otherwise have deterred it from self-reporting its material misconduct.

For a discussion of why it is important for enforcement officials to set forth, in a publicly available resolution, the factual basis for an enforcement action, the justifications for the form of resolution used, the sanctions imposed and other consequences of the nontrial resolution, as well as other factors, see § 6.02, Comments *b*-*d*.

e. Disgorgement, restitution, and remediation. Civil and administrative nontrial resolutions with organizations that engaged in material misconduct should ensure that the organizations undertake full disgorgement, restitution, and remediation in accordance with §§ 6.02 and 6.07.

f. Organizational cooperation and accountability of individuals who are responsible for knowingly or intentionally causing an organization to commit material misconduct. In accordance

with § 6.03, in order to obtain credit for full cooperation, organizations should investigate and provide enforcement officials with the identity of and all information reasonably available about the individuals responsible for the misconduct. These actions can help deter misconduct if—but only if—civil and administrative enforcement authorities adopt a policy that their enforcement officials should pursue enforcement actions against all individuals who acted with the mental state required to prove the misconduct alleged and were substantially responsible for causing their organizations to engage in material misconduct. Enforcement authorities should seek to hold individuals responsible for their knowing or intentional misconduct, even in situations in which the individuals cannot pay substantial penalties. The imposition of liability on individual wrongdoers can operate as a deterrent. It also expresses society's condemnation of the individuals' misconduct and informs the public about the individuals' responsibility for their misconduct. Such enforcement actions also can result in the individuals being subject to collateral consequences. For further discussion of individual liability, see § 6.03.

g. Factual findings in agreements with organizations not binding on individuals implicated in the misconduct. Enforcement officials should adopt clear rules or guidelines specifying that factual findings contained in an agreement with an organization are binding only on the parties to the agreement and do not constitute adjudicated facts for purposes of determining the legal responsibility of individuals who are not parties to the agreement. Express provisions are needed given the multinational nature of enforcement and the potential for other countries to treat a resolution with an organization as admissible evidence of the facts of the misconduct in a case against the individuals.

h. Policy governing organization's inability to pay. See § 6.20, Comment *f*.

REPORTERS' NOTES

a. Enforcement policies. See Reporters' Notes following § 6.02.

b. Federal policies governing civil and administrative nontrial resolutions. Many federal agencies have adopted policies governing nontrial resolutions specifically aimed at the circumstances under which an organization should be eligible for a form of resolution, such as a deferred prosecution agreement (DPA), that enables it to avoid the presumptive or mandatory collateral consequences that otherwise could be triggered by an adjudicated civil or administrative enforcement action. See, e.g., DIV. OF ENFORCEMENT, SEC. & EXCH. COMM'N, ENFORCEMENT MANUAL § 6.2.3. (2012), https://www.sec.gov/divisions/enforce/enforcementmanual.pdf; CRIMINAL DIV., U.S. DEPT. OF JUSTICE; ENF'T DIV., SEC. & EXCH. COMM'N, FCPA: A RESOURCE

GUIDE TO THE U.S. FOREIGN CORRUPT PRACTICES ACT 78-79 (2nd ed. 2020) (discussing the Securities and Exchange Commission's policy on and use of DPAs and non-prosecution agreements [NPAs] in Foreign Corrupt Practices Act cases); James McDonald, Dir., Div. of Enf't, Commodity Futures Trading Comm'n, Perspectives on Enforcement: Self-Reporting and Cooperation at the CFTC, Speech at the NYU Program on Corporate Compliance & Enforcement/Institute for Corporate Governance & Finance (Sept. 25, 2017), https://www.cftc.gov/PressRoom/SpeechesTestimony/opamcdonald092517; Andrew Ceresney, Dir., Div. of Enf't, Sec. & Exch. Comm'n, ACI's 32nd FCPA Conference Keynote Address (Nov. 17, 2015), https://www.sec.gov/news/speech/ceresney-fcpa-keynote-11-17-15.html (predicating DPAs and NPAs on whether the organization self-reported); see also Sec. & Exch. Comm'n, Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act and Commission Statement on the Relationship of Cooperation to Agency Enforcement Decisions, SEC Release No. 1470, 2001 WL 1301408 (Oct. 23, 2001), http://www.sec.gov/litigation/investreport/34-44969.htm; Environmental Protection Agency Audit Policy (Apr. 2000) https://www.epa.gov/compliance/epas-audit-policy (under the Environmental Protection Act audit policy, the Environmental Protection Agency [EPA] generally will not recommend criminal sanctions, will reduce penalties, and will not request routine audit reports if the organization:

> (a) discovered the misconduct through an environmental audit or through its compliance-management system;
>
> (b) promptly reported it before the EPA detected or was likely to detect the misconduct; (c) corrected the violation;
>
> (d) took steps to prevent its recurrence; and
>
> (e) cooperated, provided the violation did not threaten serious harm.

Some of these policies treat self-reporting as one of many factors for the enforcing agency to consider when evaluating whether to enter into a settlement on more favorable terms. Other policies provide stronger incentives for organizations to self-report by setting forth a set of benefits that are provided only to organizations that self-report and, in turn, a set of negative terms (e.g., higher sanctions and an enhanced probability of a monitor) that organizations are more likely to face if they detect and do not self-report. The Securities and Exchange Commission moved in this direction in 2015 when it announced that organizations are eligible for DPAs and NPAs only if they self-report (as discussed below), Ceresney, ACI's 32nd FCPA Conference Keynote Address.

In 2017, the Commodity Futures Trading Commission announced a policy intended to promote self-reporting that offers more favorable terms to organizations that self-report, cooperate, and remediate than are available to those that only cooperate and remediate. See McDonald, Perspectives on Enforcement: Self-Reporting and Cooperation at the CFTC,; see also Vincent A. McGonagle, Acting Dir., Div. of Enf't, Commodities Futures Trading Comm'n, Memorandum on Recognizing Cooperation, Self-Reporting, and Remediation in Commission Enforcement Orders (Oct. 29, 2020), https://www.cftc.gov/PressRoom/PressReleases/8296-20.

§ 6.23. Traditional Declinations and Decisions Not to Pursue an Enforcement Action

(a) Enforcement officials should decline to pursue an enforcement action if they determine that:

(1) they do not have, and would be unlikely to obtain through a full and thorough investigation, sufficient evidence to establish that the organization violated the law; or

(2) the misconduct is not material, as defined in § 6.01(s), or otherwise does not warrant an enforcement action.

Comment:

a. Relevance of Comment following § 6.17. The Comment following § 6.17 also is relevant to § 6.23.

b. Declinations versus no action. Civil and administrative enforcement officials who decide not to pursue an enforcement action can make a formal determination that the authority will not pursue the action. This is a declination. Alternatively, the enforcement officials may simply decide that they do not want to pursue the action at this point in time (e.g., because of insufficient evidence), while reserving their ability to pursue the action later if circumstances change.

In situations in which an enforcement authority has made public its investigation of an organization for potential misconduct, enforcement officials should, in the interests of justice, publicly disclose any formal determination that they are not going to pursue the enforcement action. In situations in which the agency has not made such a formal determination and the investigation is ongoing, such a disclosure is not warranted. When a publicly disclosed investigation has been suspended and is unlikely to be restarted, enforcement officials should, in the interests of fairness, make a public announcement of the fact that the investigation has been suspended so that the organization, its shareholders, its counterparties, and others can better assess the likelihood that the organization will be sanctioned for the misconduct for which it was being investigated.

REPORTERS' NOTES

a. Relevance of Reporters' Notes following § 6.17. The Reporters' Notes following § 6.17 also are relevant to § 6.23.

§ 6.24. Choice of Nontrial Resolution When an Adjudicated Resolution Could Trigger Collateral Consequences in the United States or Abroad

(a) An organization that engaged in knowing or intentional material misconduct should presumptively be offered a nontrial resolution that finds the organization culpable for the misconduct and is not structured to avoid triggering mandatory, presumptive, or permissive collateral consequences for the organization, except as provided in subsections (b) and (c).

(b) An organization that engaged in knowing or intentional material misconduct should presumptively be offered a nontrial resolution that is structured to avoid triggering mandatory, presumptive, or permissive collateral consequences for the organization in the United States or abroad if the organization:

(1) engaged in full corrective action in accordance with §§ 6.01(n), 6.04, 6.05, and 6.07;

(2) fully cooperated in accordance with § 6.05 and undertook full disgorgement, restitution, and remediation in accordance with § 6.07, or

(3) undertook full disgorgement, restitution, and remediation in accordance with § 6.07 and engaged in substantial material cooperation which, while not fully in accordance with § 6.05, provided enforcement officials with material evidence that they otherwise did not have, and could not readily obtain, about:

(A) the full extent of the organization's knowing or intentional material misconduct or

(B) about the identity and culpability of all employees—including all high-level or substantial authority personnel—who:

(i) knowingly participated in committing, conspiring to commit, attempting to commit, or aiding and abetting the commission of the misconduct;

(ii) knowingly participated in undermining efforts to detect or investigate the misconduct, or failed to intervene to terminate it or report it to appropriate authorities within the organization after becoming aware of it; or

(iii) were willfully blind to the misconduct.

(c) An organization that engaged in knowing or intentional material misconduct should presumptively be offered a nontrial resolution that is structured to avoid triggering mandatory, presumptive, or permissive collateral consequences for the organization in the United States or abroad, even if it has not satisfied the requirements of subsection (b), if, but only if:

(1) imposing collateral consequences on the organization would likely cause material harm to consumers, employees in units of the organization that were not involved in the misconduct, or the public, and the magnitude of that harm would exceed the likely benefits of imposing collateral consequences given the availability of other means for reducing the organization's future risk of misconduct, such as appointing a compliance monitor;

(2) the organization has fully remediated in accordance with § 6.07 or will be required to fully remediate in accordance with § 6.09; and

(3) one of the following conditions is satisfied:

(A) the organization did not fully cooperate based on a good-faith belief, predicated on a reasonable interpretation of the law, that it did not engage in misconduct;

(B) the nontrial resolution requires an organization that did not have an effective compliance program at the time it knowingly or intentionally engaged in material misconduct to accept and pay for oversight by a compliance monitor (in accordance with §§ 6.10–6.12); or

(C) the organization had an effective compliance program at the time of the misconduct, in accordance with Chapter 5.

(d) A nontrial resolution structured to avoid collateral consequences because the organization engaged in full corrective action in accordance with § 6.01(n) should presumptively not impose a monitor on the organization, even if aggravating circumstance were present, consistent with §§ 6.10–6.12.

Comment:

a. Full corrective action. In accordance with § 6.01(n), the term "full corrective action" refers to an organization taking the following steps: self-reporting its material knowing or

intentional misconduct (in accordance with § 6.04), fully cooperating with enforcement officials (in accordance with § 6.05), *and* engaging in timely and full disgorgement, restitution, and remediation (in accordance with § 6.06). An organization has undertaken full corrective action if it has either already engaged in or has committed to engaging in the conduct necessary to comply with §6.01(n). An organization that has committed to satisfying § 6.01(n) in a nontrial resolution but later fails to do so in a material way would be in breach of the agreement.

b. Material misconduct. The standard for a material misconduct is provided in § 6.01(s) and Comment *h* to that Section.

c. Full cooperation and full remediation. For a discussion of full cooperation and remediation, disgorgement, and restitution, see §§ 6.05 & 6.07.

In assessing whether an organization undertook full disgorgement, restitution, and remediation in accordance with § 6.07, enforcement officials should ensure that:

(1) the organization promptly terminated all detected misconduct;

(2) the organization has undertaken any reforms needed to implement an effective compliance program; and

(3) all high-level or substantial authority personnel who knowingly participated in committing the offense, knowingly participated in undermining detection or investigation of the offense, or knew about material misconduct and failed to intervene to terminate it or report it to appropriate authorities within the organization after becoming aware of it, are no longer in positions of authority with the organization.

An organization should be determined to have complied with §§ 6.05 or 6.07 if it has already taken steps to satisfy or has committed in good faith to taking steps to satisfy §§ 6.05 or 6.07, respectively. An organization that commits in a nontrial resolution to satisfying §§ 6.05 or 6.07 but later fails to do so in a material way would be in breach of the agreement.

d. Presumptions, not mandatory guidelines. The Principles in this Section are phrased as presumptions to guide civil and regulatory enforcement officials when making decisions as to the appropriate form of nontrial resolution for organizations.

By establishing presumptions to guide enforcement decisions, enforcement authorities promote deterrence and transparency because the presumptions enable organizations to predict how their conduct will impact the form of resolution. By establishing presumptions, enforcement authorities also promote consistency in the use of various forms of nontrial resolution among the

enforcement officials governed by the presumptions. This enables enforcement officials the ability to offer favorable forms of nontrial resolutions to induce both self-reporting and cooperation. It also enables them to use their selection of the form of nontrial resolution to publicly differentiate organizations that acted proactively to help deter misconduct and enforce the law from those that did not.

Enforcement officials retain discretion to deviate from the recommendations in this Section in situations in which they conclude that a different form of resolution than is recommended by this Section would better serve the goals of civil or administrative enforcement against organizations. A nonexclusive list of factors that enforcement officials can take into account, beyond those upon which the presumptions are predicated, include:

(1) the size of the organization;

(2) the role of the organization's owners in committing or condoning the offense;

(3) the form of organization, including whether it is for-profit or nonprofit;

(4) the value to enforcement officials of the organization's cooperation;

(5) the type of offense (for example, whether the offense involved fraud or material harm to others); and

(6) whether the delay or costs associated with a trial would harm enforcement officials' ability to achieve justice because, for example:

(A) important witnesses may no longer be available (e.g., for health reasons);

(B) the misconduct was not substantial enough to justify the cost and delay of a trial; or

(C) a nontrial resolution that does not require admissions would better enable enforcement officials to: cause the organization to promptly terminate and remediate misconduct that risks material future harm to persons or property or to provide prompt restitution to victims who were materially injured by the misconduct.

While enforcement officials have discretion in determining the appropriate form of resolution, this Section reflects the view that the following considerations do not, in and of themselves, justify using a nontrial resolution structured to avoid collateral consequences in cases in which an organization engaged in knowing or intentional material misconduct and did not satisfy the conditions set forth in § 6.24(b) and (c): (1) the desire for a prompt resolution (absent

additional factors supporting a conclusion that promptness would serve a material social interest); and (2) concern about the collateral consequences of enforcement on shareholders or management.

Collateral consequences alone do not justify an adjustment to the form of nontrial resolution, except as provided in § 6.24(b) & (c), because, throughout the negotiation process, an organization retains the ability to obtain the more favorable treatment needed to avoid collateral consequences by providing the requisite cooperation. An organization that persists in refusing to cooperate or fully remediate should not be protected from the adverse consequences of its decision to do so.

e. Guidelines governing the use of resolutions that do not trigger mandatory, presumptive, or permissive collateral consequences. Section 6.24 focuses on the decision whether to use a form of nontrial resolution that could trigger mandatory, presumptive, or permissive collateral consequences in the United States or abroad, instead of on the choice between specific forms of nontrial resolutions or remedies. The reason for this is that in the civil and administrative enforcement context, there is not a specific set of nontrial resolutions and/or remedies that generally trigger collateral consequences across all civil and administrative enforcement authorities and another set that do not, as is the case in the criminal context. In the civil and administrative enforcement context, different forms of nontrial resolution, and different remedies contained in a nontrial resolution, can trigger collateral consequences depending on: (1) the industry in which the organization operates; (2) the civil, administrative, or self-regulatory authority with jurisdiction over the organization; and (3) the type of misconduct involved.

Nontrial resolutions for knowing or intentional civil misconduct can trigger mandatory, presumptive, or permissive collateral consequences under many, but not all, statutes. In addition, some agencies impose collateral consequences on organizations that were subject to certain remedies, such as an injunction against future violations of specific laws or an order requiring that the organization cease and desist from violating specific laws. Administrative agencies and self-regulatory authorities often can waive collateral consequences.

This Section uses the term “no collateral consequences” resolution to refer to nontrial resolutions that are structured to avoid collateral consequences that otherwise could result from an adjudicated resolution or a resolution that imposes certain direct consequences, such as an injunction.

f. Enforcement guidelines structured to reduce knowing or intentional material misconduct by incentivizing full corrective action or full cooperation. Civil and regulatory enforcement serves many goals including preventing, deterring, and remediating misconduct; rehabilitating organizations that have engaged in misconduct; providing restitution to victims; and providing credible information to the public about organizations that engaged in misconduct.

In the case of knowing and intentional misconduct by large organizations, enforcement authorities can most effectively deter, terminate, and remediate misconduct if they are able to expeditiously detect and terminate it, ensure that the organization disgorges any benefit from the misconduct, and are able to obtain in a reasonable time the evidence needed to bring the individuals responsible for the misconduct to justice. Enforcement policies that ensure that organizations always must disgorge the benefit of their employees' misconduct promotes deterrence by providing firms with a profit-oriented motivation to deter their employees' misconduct. Enforcement policies that ensure full remediation also enhance organizations' ability to deter misconduct. Enforcement policies that promote prompt detection and full cooperation help deter to the extent they cause employees contemplating misconduct to face a material and salient risk that the organization would detect and report any misconduct they commit and provide enforcement authorities with sufficient evidence to sanction the employees.

These actions also can enable them to obtain restitution for victims and promoting rehabilitation of organizations. Enforcement authorities often can best achieve these goals by providing organizations with substantial incentives to self-report and cooperate, however. Enforcement authorities thus should structure their enforcement policies to induce organizations to self-report, fully cooperate and remediate and should avoid policies that would deter such actions in pursuit of objectives other than deterrence. A decision to reduce the deterrent effect of enforcement can be expected to lead to more misconduct and more public harm.

Accordingly, civil and administrative enforcement authorities should adopt and publicly disclose their policies that govern how they chose nontrial resolutions for organizations that have engaged in knowing or intentional material misconduct. These policies should be designed to provide organizations with substantial incentives to self-report and cooperate for the reasons given in § 6.02, Comment *f*.

Civil and regulatory enforcement authorities also should structure their enforcement policies to provide strong incentives for organizations to fully cooperate. Of particular importance,

enforcement authorities should ensure that organizations: (1) thoroughly investigate detected material misconduct, ascertain its full scope, and share information, including evidence found during the investigation, with enforcement authorities; and (2) identify the individuals responsible for the misconduct and provide enforcement authorities with evidence relating to their involvement, in accordance with § 6.05. By cooperating, organizations also may enable enforcement authorities to expeditiously detect, terminate, and ensure remediation of additional misconduct that had not been detected by the government. A policy that promotes full cooperation also promotes deterrence, rehabilitation, and restitution by enabling enforcement authorities to pursue appropriate actions against organizations and individuals. Employees should be deterred from engaging in misconduct if they expect their organization to proactively strive to detect and investigate misconduct and to provide the resulting evidence about employees' misconduct to the government.

Organizations generally will not self-report misconduct or provide prompt and full cooperation that supplies civil or administrative enforcement officials with evidence that can be used against them unless they have a substantial reason to do so. To provide such incentives, civil and regulatory enforcement officials should ensure that organizations are aware that: (1) they can obtain a resolution that avoids collateral consequences if they undertake these actions; and (2) they will not be able to resolve a case of material misconduct through a resolution structured to avoid collateral consequences if they neither self-report nor cooperate in accordance with either or § 6.24(b), except as provided in § 6.24(c).

Accordingly, to ensure that organizations are confident that they will be offered a form of nontrial resolution that does not trigger mandatory, presumptive, or permissive collateral consequences if they either (1) undertake full corrective action or (2) fully cooperate and remediate in accordance with §§ 6.05 and 6.07, enforcement officials should adopt a presumption that an organization that undertakes full corrective action or that undertakes full cooperation and full disgorgement, restitution, and remediation will be able to resolve a matter through a form of nontrial resolution that does not trigger presumptive or mandatory collateral consequences, in the United States or abroad.

Such a presumption will not operate to provide strong incentives for organizations to self-report or fully cooperate, however, if organizations also can readily resolve cases involving knowing or intentional material misconduct through forms of nontrial resolution designed to avoid

collateral consequences even if they do not self-report or fully cooperate. When an organization can readily obtain leniency by agreeing to settle promptly or taking other actions that do not involve self-reporting or cooperation, a presumption favoring a no-collateral consequence resolution for organizations that self-report or fully cooperate will provide little incentive for the organization to undertake such actions.

Accordingly, § 6.24 establishes a presumption that enforcement officials should *not* offer a nontrial resolution designed to avoid collateral consequences unless the organization satisfies either subsection (b) or (c). Thus, an organization should not be eligible for a no-collateral-consequence form of resolution based on nothing more than its willingness to promptly settle the case, make restitution payments to victims, and undertake some internal reforms.

g. Insulating an organization from collateral consequences notwithstanding aggravating circumstances. Section 6.24 establishes a presumption in favor of resolving misconduct allegations through a nontrial resolution that does not trigger mandatory, presumptive, or permissive collateral consequences if the conditions set forth in subsections (b) or (c) are satisfied, even in cases in which the aggravating circumstances set forth in § 6.18(c) exist.

The presumption should remain in place even when aggravating circumstances are present because the presumption is needed to incentivize self-reporting, full cooperation, and remediation. When aggravating circumstances are present, it is particularly important that enforcement authorities be able to promptly detect and terminate misconduct that causes serious harm or involves managers. The presumption helps enable enforcement authorities to detect and enforce material misconduct that otherwise might remain undetected. It also better enables enforcement officials to identify organizations in need of remediation and to enter into nontrial resolutions that effectuate effective internal reforms more rapidly than they could have without the organization's cooperation. This resulting improved enforcement also can promote the goal of providing restitution to victims by ensuring that enforcement officials obtain the information they need to induce individuals and organizations to enter into nontrial resolutions for misconduct that provide redress to the individuals harmed by the misconduct. Finally, it serves the important goal of informing the public about both the nature of the organization's misconduct and the type of individuals who were responsible for it by enabling enforcement officials to more promptly detect and sanction misconduct that otherwise might have remained undetected. Thus, as long as the organization has truly satisfied § 6.24(b) by, among other actions, identifying the full scope of the

misconduct and providing all reasonably available evidence against those responsible for it, the organization should be confident of avoiding collateral consequences even though the misconduct caused serious harm or involved senior management, or even if the organization was previously involved in misconduct.

While aggravating circumstances should not negate the presumptions set forth in § 6.24 (b) and (c), they may be relevant to other aspects of the nontrial resolution, such as sanctions and remedial measures. Enforcement officials can address aggravating circumstances that indicate that an organization has an enhanced risk of engaging in future misconduct through measures aimed directly at this risk, such as the appointment of a compliance monitor.

h. Less-than-full cooperation. Section 6.24 establishes a presumption that an organization should not be eligible for a nontrial resolution structured to avoid imposing mandatory, presumptive, or permissive collateral consequences unless the organization both fully cooperated (in accordance with § 6.05) and undertook full disgorgement, restitution, and remediation in accordance with § 6.07.

However, the Section provides two exceptions to this presumption: subsections (b)(3) and (c) (addressed in Comment *i*).

Subsection (b)(3) states that an organization can obtain a nontrial resolution that does not trigger collateral consequences, even if it did not fully cooperate, if the organization provided enforcement officials with material evidence that they otherwise did not have, and could not readily obtain, about:

(A) the full extent of the organization's knowing or intentional material misconduct and (B) the identity and culpability of all employees—including all high-level or substantial authority personnel—who:

(i) knowingly participated in committing, conspiring to commit, attempting to commit, or aiding and abetting the commission of the offense;

(ii) knowingly participated in undermining detection or investigation of the offense;

(iii) failed to intervene to terminate it or report it to appropriate authorities within the organization after becoming aware of it; or

(iv) were willfully blind to the misconduct.

The exception provided in subsection (b)(3) recognizes that civil and administrative enforcement authorities regularly face substantial resource challenges in investigating knowing or

intentional material misconduct. Many civil and administrative enforcement authorities do not have sufficient resources to detect or promptly pursue effective enforcement actions against most of the misconduct under their jurisdiction. In light of these challenges, enforcement authorities can promote the goals of deterrence, rehabilitation, and restitution to victims by offering no-collateral consequences nontrial resolutions to organizations that did not fully cooperate, so long as the organization:

(1) provided enforcement officials with substantial material cooperation involving evidence enforcement officials did not already have—and would be unlikely to readily obtain—about the scope of it misconduct and identity of the individuals responsible for the misconduct and their roles in it; and

(2) undertook full disgorgement, restitution, and remediation (in accordance with § 6.07). The requirement that the organization fully remediate includes a requirement it ensures that all employees who were knowingly responsible for the organization's failure to fully cooperate are no longer in positions of authority with the organization.

i. Disproportionate collateral consequences. Section 6.24(c) states that, notwithstanding an organization's failure to satisfy § 6.24(b), enforcement officials should offer to resolve a case involving knowing or intentional material misconduct through a nontrial resolution that avoids triggering collateral consequences if, but only if, three conditions are met. First, subsection (c) is limited to situations in which the collateral consequences would harm innocent parties such as customers (e.g., patients who purchase pharmaceuticals from the organization) or employees in organizational units that were not involved in the misconduct. The term "innocent parties" does not refer to shareholders because otherwise every publicly held firm would be able to avoid collateral consequences without satisfying § 6.24(b).

Second, the organization must undertake full remediation in accordance with § 6.07. Collateral consequences can be an important tool for reducing the risk that an organization will cause future harm (as discussed in § 6.26). Accordingly, an organization that is otherwise subject to collateral consequences should undertakes full remediation that is designed to address the root causes of its misconduct. Full remediation entails taking appropriate actions to ensure that any officials in the organization who are knowingly responsible for either the organization's misconduct or its failure to fully cooperate are no longer in positions of authority.

Finally, enforcement officials should determine whether the organization's failure to fully cooperate and remediate provided a basis for concluding that the organization has a heightened risk of future misconduct. An organization evidences a lack of commitment to deterring and remediating misconduct if it fails to fully cooperate and remediate with respect to knowing or intentional misconduct about which it is aware. Accordingly, this Section creates a presumption that enforcement officials should impose a compliance monitor on any an organization as a precondition of it obtaining a nontrial resolution that avoids collateral consequences pursuant to § 6.24(c)(3) unless the organization had an effective compliance program at the time of the misconduct or was justified in its initial failure to cooperate. An organization is justified in its initial failure to fully cooperate if it can establish that its decision not to investigate or cooperate was predicated on a reasonable good-faith belief, based on a reasonable interpretation of the law, that it did not engage in misconduct. This exception applies only when the organization does not have notice that the civil or regulatory enforcement authority has a good faith, reasonable interpretation of the law under which the organization violated the law. When an enforcement authority offers an organization a nontrial resolution that avoids triggering collateral consequences based on the fact that organization believed reasonably and in good faith that it did not violate the law, the resolution should explicitly set forth basis for the organization's legal conclusion that it did not violate the law and the basis for the enforcement authority's conclusion that it did violate the law.

By contrast, if the organization lacked justification for its failure to cooperate, an enforcement authority can justifiably infer that the organization is not fully committed to deterrence and to complying with the law in the future. In this situation, enforcement officials should only offer a no-collateral consequences resolution to an organization that did not satisfy § 6.24(b) if they impose a compliance monitor on the organization, in accordance with §§ 6.10-6.12. An organization's unjustified failure to fully cooperate in accordance with § 6.05 provide a strong factual basis for enforcement authorities to conclude that its management cannot be relied on to either ensure the organization will comply with the law or fully remediate the harm that it caused. If an organization did not have an effective compliance program in place at the time of the misconduct, a monitor should be appointed. However, a monitor may not be necessary if the organization had an effective compliance program at the time of the misconduct and the misconduct was an isolated event that did not involve high-level or substantial authority personnel.

In addition, when seeking to ensure that the organization fully remediates the root causes of the misconduct and the organization's compliance deficiencies, enforcement officials should ensure that the the organization removes from positions of authority all individuals who were knowingly and materially responsible for either the misconduct or for the organization's unjustified refusal to cooperate.

This Section does not permit an organization to obtain a resolution that avoids collateral consequences simply by asserting that the costs of the collateral consequences would be ruinous. Collateral consequences are aimed at protecting the public and others from an organization that presents a high risk of misconduct. When an organization commits knowing or intentional misconduct and then unjustifiably fails to provide the cooperation and remediation set forth in § 6.24(b)(3), the facts favor imposing collateral consequences in accordance with § 6.26. An organization that wants to avoid such collateral consequences should act in accordance with § 6.07 and cooperate consistent with § 6.24(b)(3).

j. Benefits of adopting and implementing an effective compliance program. Enforcement authorities should not offer a no-collateral consequences resolution to an organization that engaged in knowing or intentional material misconduct, but did not satisfy § 6.24(b) or (c), even if the organization had an effective compliance program. An effective compliance program is not, in and of itself, a sufficient basis for obtaining a nontrial resolution that avoids collateral consequences for the reasons discussed in the context of criminal prosecution in § 6.17, Comments *c* & *d*. The only exception to this general rule in the context of civil and administrative enforcement is when the organization's liability under a statute or regulations is predicated on its failure to adopt or maintain an effective compliance program to address a particular legal risk (e.g., money-laundering).

While this Section does not predicate access to a no-collateral consequences resolution on an effective compliance program, this Topic both recognizes that effective compliance programs are valuable and provides material incentives for organizations incentives to adopt and implement an effective compliance program. This Section provides direct incentives for organizations to adopt an effective compliance program that helps detect and obtain evidence about misconduct by offering substantial benefits to organizations that self-report and cooperate. In addition, an organization's adoption and maintenance of an effective compliance program is an important consideration in determining: (1) the magnitude of the penalty imposed; (2) whether mandated

internal reforms should be required in accordance with § 6.09; and (3) whether the nontrial resolution should impose a monitor in accordance with §§ 6.10–6.12.

k. Collateral consequences. For discussion of the impact of collateral consequences on the form of a criminal nontrial resolution see § 6.17, Comment *e*.

l. Application to small, owner-managed, closely held organizations. Small, owner-managed, closely held organizations make up the bulk of the cases in which enforcement authorities have detected misconduct. Owner-managers regularly are implicated in, or their actions are the underlying precipitating cause of, misconduct committed by such organizations, especially when the misconduct involved violations of environmental, worker-safety, immigration, and tax laws. However, because owner-managers regularly take steps to avoid directly committing an unlawful act, often the only way of seeking recourse is to hold the organizations liable. Organizational liability combined with collateral consequences can be a particularly important tool for ensuring that owner-managers who knowingly allow their organizations to engage in material misconduct are both punished and prevented from engaging in future violations.

The presumptions in this Section are unlikely to result in such organizations becoming eligible for a no-collateral-consequences resolutions for their misconduct when their owners are implicated for two reasons. First, implicated owner-managers of closely held companies are unlikely to allow their firms to self-report and fully cooperate since such actions could put the owner-managers in peril. Second, implicated owner-managers will not undertake full remediation in accordance with § 6.07, as is required by this Section, because such remediation would threaten their jobs, as it requires that the organizations identify, discipline, and possibly dismiss all high-level personnel who caused or knowingly condoned the misconduct.

Whether small or closely held organizations that are not owner-managed are good candidates for no-collateral-consequences resolutions of their misconduct likely depends on whether the boards of directors and senior management of such organizations are sufficiently independent of those involved in the misconduct that they are willing to self-report, fully cooperate, and fully remediate. A family-owned organization is unlikely to take such steps when a family member is implicated in the misconduct. This Section should encourage self-reporting and full cooperation by private organizations whose owners and boards of directors are independent of those individuals implicated in the misconduct.

m. Recidivism. The presumption of § 6.24(b) applies to organizations that previously engaged in misconduct. Enforcement authorities benefit from using the presumption to induce organizations to self-report and fully cooperate, regardless of whether the organization previously engaged in misconduct. In addition, an organization's past misconduct need not indicate that it fails to take its legal obligations seriously. Very large organizations that operate in heavily regulated sectors face the omnipresent risk that an employee will violate the law even if the organization has adopted and maintains an optimal compliance program. Accordingly, in order to ensure that all organizations have material incentives to undertake full corrective action or to fully cooperate and undertake full disgorgement, restitution, and remediation, Section 6.24 applies to all organizations.

The concern that this approach might cause organizations to be overly willing to violate the law in a quest for profits, confident of their ability to satisfy § 6.24, is addressed in three ways. First, sanctions should be adjusted to reflect past knowing or intentional material misconduct of a similar type. Second, managers contemplating such an approach should be deterred by appropriate application of § 6.07, which exhorts enforcement authorities to ensure that organizations remediate the root causes of their misconduct, including by taking appropriate actions with respect to supervisors who encouraged, induced, or condoned the misconduct. Finally, organizations that repeatedly violate the law are more likely, depending on other factors, to be a good candidates for mandated internal reforms, in accordance with § 6.09, and the appointment of a compliance monitor, in accordance with §§ 6.10–6.12. For a discussion of criminal recidivism see § 6.18, Comment *j*.

n. Legal duty to self-report. Section 6.24 is predicated on the assumption that organizations do not have a legal obligation to self-report misconduct. When organizations do have a legal duty to report either misconduct or a risk of harm, enforcement officials should proactively pursue enforcement actions against those that do not self-report when they were legally required to do so. An organization nevertheless can be presumptively eligible for a no-collateral consequences resolution if it satisfied § 6.24(b) and if it took actions, such as fully cooperating or remediating, that it was not legally required to take.

o. Importance of individual enforcement actions. Enforcement officials entering into no-collateral consequences resolutions for knowing or intentional material misconduct should undertake their best efforts to pursue civil or administrative enforcement against individuals who

knowingly or intentionally committed, attempted to commit, or aided and abetted or conspired to commit material misconduct, if they were substantially responsible for the misconduct and are appropriately held liable for it in the United States, in accordance with § 6.03. They also should refer such individuals to prosecutors. If a case involving knowing or intentional material misconduct is resolved through a no-collateral consequences resolution with the organization, but no civil or regulatory action is taken against any individuals who knowingly or intentionally engaged in the misconduct, that would be inconsistent with the central policy justifications for no-culpability resolutions with organizations.

p. No collateral consequences resolution versus a declination with disgorgement. Section 6.24 adopts the presumption that an organization that engaged in knowing or intentional material misconduct should be subject to a civil or administrative enforcement action even if the organization undertook full corrective action. A civil or administrative enforcement action provides important public notice about the facts of the misconduct and the steps taken to remediate it. It also can be needed to ensure that the organization does not retain the benefit of misconduct, among other goals. Nevertheless, there are circumstances in which deterrence and the interests of justice may best be served through a policy that offer organizations that undertake full corrective action–and only those organizations—a declination with disgorgement (consistent with § 6.18). Such a policy may be appropriate in circumstances in which the threat of a public nontrial resolution that sanctions an organization for knowing or intentional misconduct would deter organizations subject to an enforcement authorities' jurisdiction from self-reporting and full cooperating with respect to material misconduct that enforcement authorities would be unlikely to detect on their own even if the resolution were structured in accordance with § 6.24 and 6.25. This is particularly likely if the resolution could result in the organization incurring substantial costs imposed by other public authorities (domestic or foreign) or private litigation. When enforcement authorities can best protect the public by inducing prompt self-reporting, then a policy favoring a declination with disgorgement in accordance with the requirements of § 6.18 may be appropriate. Such a policy can also promote the interests of victims through provisions requiring full disgorgement, restitution, and remediation in accordance with § 6.07 as a precondition of obtaining a declination with disgorgement.

r. Relevance of the Comments in Topic 3. The Comments in Topic 3 relating to the policies governing the choice between guilty pleas, declinations with disgorgement, DPAs, and NPAs also

are relevant to civil and regulatory enforcement authorities' policies governing the choice between a civil or administrative enforcement action (seeking a judicial decree or order that the company violated the law) on the one hand, and a form of nontrial resolution that either does not trigger collateral sanctions (such as a DPA or NPA) or does not require the organization to admit to all the facts of the misconduct, on the other. See §§ 6.15–6.19.

REPORTERS' NOTES

a. Policy of federal regulators on the impact of self-reporting on the form of the enforcement action. The Securities and Exchange Commission (SEC), Commodity Futures Trading Commission (CFTC), and the U.S. Department of Justice, Antitrust Division (Antitrust Division) each have adopted policies under which organizations may be able to obtain leniency if they self-report or cooperate, and remediate. Leniency under these policies either takes the form of a declination or of a nontrial resolution that would not trigger collateral consequences. Some of these programs treat self-reporting as one of many factors to consider when evaluating whether to enter into a settlement on more favorable terms. Other programs provide stronger incentives to self-report by setting forth a set of benefits that are only provided to organizations that self-report, and in turn a set of negative terms (e.g., higher sanctions and an enhanced probability that a monitor will be appointed) that organizations are more likely to face if they detect and do not self-report. For a discussion of these policies see the Reporters' Notes below and § 6.18, Reporters' Note f.

b. SEC policy regarding organizational nontrial resolutions and the use of DPAs and NPAs. The SEC adopted its original policy on organizational leniency in the Seaboard Report. See Sec. & Exchange Comm'n, Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act and Commission Statement on the Relationship of Cooperation to Agency Enforcement Decisions, SEC Release No. 1470, 2001 WL 1301408 (Oct. 23, 2001), http://www.sec.gov/litigation/investreport/34-44969.htm. In the Seaboard Report, the SEC explained its decision not to pursue an enforcement action against a public company for certain accounting violations caused by its subsidiary, detailing the factors that supported leniency. The report identified four important considerations: (1) self-reporting of detected misconduct; (2) remediation (including dismissing or appropriately disciplining wrongdoers) and improvements to the organization's compliance program; (3) full cooperation; and (4) maintenance of an effective compliance program prior to the discovery of the misconduct.

In 2010, the SEC announced a policy of encouraging full cooperation through the use of deferred prosecution agreements (DPAs), non-prosecution agreements (NPAs), and other alternatives to formal enforcement. Sec. & Exchange Comm'n, SEC Announces Initiative to Encourage Individuals and Companies to Cooperate and Assist in Investigations, SEC 10-6, 2010 WL 109926 (Jan. 13, 2010), https://www.sec.gov/news/press/2010/2010-6.htm. The SEC's Enforcement Manual identifies four measures of a company's cooperation: (1) self-policing prior to the company's discovery of the misconduct; (2) self-reporting after discovering the misconduct; (3) remediation of the misconduct; and (4) cooperation with law enforcement. The Enforcement

Manual identifies a continuum of tools designed to reward cooperation from proffer and cooperation agreements, to DPAs and NPAs, to criminal immunity requests. See DIV. OF ENFORCEMENT, SEC. & EXCH. COMM'N, ENFORCEMENT MANUAL § 6.1.2 (2017), https://www.sec.gov/divisions/enforce/enforcementmanual.pdf.

Although the initial policy enabled companies to obtain a DPA or NPA without self-reporting, on Nov. 17, 2015, the SEC announced a new policy that requires companies to self-report Foreign Corrupt Practices Act violations in order to be eligible to settle through a DPA or NPA. Andrew Ceresney, Dir., Div. of Enf't, Sec. & Exch. Comm'n, ACI's 32nd FCPA Conference Keynote Address (Nov. 17, 2015), https://www.sec.gov/news/speech/ceresney-fcpa-keynote-11-17-15.html.

It might appear that DPAs and NPAs do not serve the same purpose when implemented by the SEC as they do in the criminal context because SEC commissioners have authority to simultaneously settle enforcement actions and ensure that the organization is not subject to most collateral consequences imposed by the commission. See § 6.21, Reporters' Note *b*. In fact, officials in the SEC's enforcement division can benefit from adopting a policy regarding DPAs and NPAs that offers companies access to these forms of resolution if, but only if, they self-report and cooperate, for two reasons. First, such settlements would not trigger those collateral consequences that the SEC does not have authority to waive. For example, a company is not eligible for the safe harbor if it:

(1) was convicted of a felony or certain misdemeanors; or

(2) was made the subject of a judicial or administrative decree or order arising out of a governmental action that:

(a) determines that the issuer violated;

(b) requires that the issuer cease and desist from violating; or

(c) prohibits future violations of, the antifraud provisions of the securities laws.

15 U.S. C. § 78u-5(b).

Second, such settlements allow the SEC's Enforcement Division to provide strong incentives to companies to self-report and cooperate in order to obtain a DPA or NPA, because the Enforcement Division cannot guarantee that the SEC will waive collateral consequences on a company that is subject to a formal enforcement action. This is because the recommendation of whether collateral consequences should be imposed is made by SEC officials in a different division of the SEC, prior to ultimate referral to the SEC. In addition, as with criminal DPAs and NPAs, SEC DPAs and NPAs can insulate organizations from collateral consequences imposed by other authorities that could be triggered by the SEC imposing civil penalties for fraud-related misconduct. James McDonald, Dir., Div. of Enf't, Commodity Futures Trading Comm'n, Perspectives on Enforcement: Self-Reporting and Cooperation at the CFTC, Speech at the NYU Program on Corporate Compliance & Enforcement/Institute for Corporate Governance & Finance (Sept. 25, 2017), https://www.cftc.gov/PressRoom/SpeechesTestimony/opamcdonald092517.

c. CFTC policy regarding nontrial resolutions with organizations and the use of DPAs. In 2017, the CFTC announced a policy intended to promote self-reporting by offering more favorable terms to organizations that self-report, cooperate, and remediate than those that are available to organizations that only cooperate and remediate. McDonald, *Perspectives on Enforcement: Self-Reporting and Cooperation at the CFTC*.

d. Antitrust Division policy on corporate nontrial resolutions and leniency. For an example of an early effort to provide predictability, see Antitrust Division Corporate Leniency Policy (offering leniency to organizations that self-report if six conditions are met, including reporting fully before the illegal activity is reported from any other source). https://www.justice.gov/atr/file/810281/download. This policy thus restricted leniency to the first company to self-report (offering leniency to organizations that self-report).

More recently, the Antitrust Division has indicated that NPAs would be reserved for such firms, but that firms that were not the first to self-report might obtain a DPA. Factors favoring a DPA include adoption and maintenance of an effective compliance program, full cooperation, and remediation. Assistant Attorney General Makan Delrahim has stated, however, that the Principles of Federal Prosecution of Business Organizations "counsel against crediting a compliance program when the other three hallmarks of good corporate citizenship are absent": specifically, (1) prompt self-reporting, (2) full cooperation with the Antitrust Division's investigation, and (3) remediation. Makan Delrahim, Assistant Att'y Gen., Antitrust Div., U.S. Dept. of Just., Wind of Change: A New Model for Incentivizing Antitrust Compliance Programs, Remarks at the New York University School of Law Program on Corporate Compliance and Enforcement (July 11, 2019), https://www.justice.gov/opa/speech/assistant-attorney-general-makan-delrahim-delivers-remarks-new-york-university-school-l-0.

e. Federal policy on the impact of an effective compliance program. See § 6.08, Reporters' Notes *f* & *g*.

f. Legal obligation to self-report. These Principles in this Topic focus on enforcement policy in the situation in which an organization is not legally required to self-report. Some organizations are subject to legal requirements to self-report some or all violations or potential harms. Self-reporting requirements are particularly common for products that could cause personal injury. These requirements also are commonly imposed on heavily regulated industries. These may be imposed by statute or regulation or by a self-regulatory authority, such as the Financial Industry Regulatory Authority.

In those situations, the existence of a duty to self-report, if adequately enforced and accompanied by adequate sanctions, may be sufficient incentive for organizations to self-report misconduct. If the duty includes a duty to investigate and fully cooperate, then organizations may undertake those activities too. Nevertheless, enforcement officials may enhance deterrence by offering more favorable settlement terms for the underlying misconduct if an organization self-reports and cooperates, especially if otherwise the sanction for the misconduct would trigger mandatory or presumptive collateral consequences, such as delicensing, debarment, or exclusion. For a discussion of how agencies should approach collateral consequences to protect their interests

while not deterring self-reporting and full cooperation, see Cindy R. Alexander & Jennifer Arlen, *Does Conviction Matter? The Reputational and Collateral Effects of Corporate Crime*, in RESEARCH HANDBOOK ON CORPORATE CRIME AND FINANCIAL MISDEALING (Jennifer Arlen ed., 2018).

g. Increased risk of unsuccessful enforcement actions and oversight by the executive branch and the legislature. Adherence to the Principle in this Section, and a commitment to reserving no-culpability nontrial resolutions for knowing or intentional material misconduct for organizations that satisfied the provisions of § 6.24, can be expected to result in situations where enforcement officials need to pursue litigation against an organization that refused to provide adequate cooperation to satisfy § 6.24. This investment is justified by the long-term benefits of providing clear and strong incentives to organizations to self-report and fully cooperate. These benefits include speedier detection of (and thus less harm resulting from) misconduct, enhanced ability to detect, terminate, and remediate the full scope of the misconduct, and enhanced deterrence resulting from increased self-reporting and cooperation, and as a result stronger enforcement actions against individuals who knowingly or intentionally commit material misconduct. Nevertheless, the effort to obtain these long-term benefits may come at a cost of fewer successful enforcement actions in any given year for two reasons. First, enforcement officials can be expected to lose some of the cases they take to trial. Second, in the short run, they also may be able to pursue fewer other actions as a result of the time spent on the litigation. This short-term decrease in successful enforcement resolutions can be expected to enable enforcement authorities to be more effective in the future and thus should be supported by other government authorities.

Civil and regulatory enforcement authorities regularly must report on their activities both to more senior officials in the executive branch (such as the office of the governor or president) and to the legislature. This reporting regularly includes information on the number of successful enforcement resolutions. The executive branch and the legislature can promote the public interest by not treating the number of successful enforcement resolutions as the measure of an enforcement authority's effectiveness and by not treating unsuccessful litigation as a presumptive indication of the enforcement authority's deficiency. They also can promote the public interest by asking enforcement authorities to provide information on the seriousness of the harm associated with the misconduct (mean, median, 25th percentile, and 75th percentile), the level of culpability (e.g., intentional misconduct versus negligence), the percentage of cases involving intentional or knowing organizational misconduct that resulted in a case being brought against an individual and the number of successful resolutions of those cases, the collateral consequences imposed against individuals, and the percentage of organizational resolutions for intentional or knowing misconduct that took the form of full-admission, partial-admission, neither-admit-nor-deny, or denial-permitted resolutions. Legislatures also can enhance deterrence by ensuring that enforcement authorities have sufficient resources to be able to pursue effective investigations and litigation in those circumstances where an organization does not fully cooperate.

h. Use of DPAs and NPAs in other countries. For a discussion of the use of DPAs, NPAs and their equivalent in other countries see § 6.04, Reporters' Note *e*; § 6.05, Reporters' Note *i*; § 6.15, Reporters' Note *e*.

i. Academic literature on DPAs and NPAs with organizations in criminal cases. For a discussion of the academic literature on the use of DPAs and NPAs in criminal cases against organizations, see § 6.15, Reporters' Note *f*; § 6.18, Reporters' Note *g*; and § 6.19, Reporters' Note *c*; see also § 6.09, Reporters' Note *d*.

j. Academic literature on the use of nontrial resolutions, including DPAs, in civil enforcement actions. Scholarship on the use of DPAs, NPAs, and other forms of nontrial resolutions in civil enforcement actions includes: Rachel Barkow, *Prosecutor as a Regulatory Agency*, in PROSECUTORS IN THE BOARDROOM: USING CRIMINAL LAW TO REGULATE CORPORATE CONDUCT 177 (A. Barkow & R. Barkow eds., 2011) (discussing the use by the New York attorney general of structured settlements in civil as well as criminal cases brought under the Martin Act); Samuel Buell, *The Potentially Perverse Effects of Corporate Civil Liability*, in PROSECUTORS IN THE BOARDROOM: USING CRIMINAL LAW TO REGULATE CORPORATE CONDUCT 62 (A. Barkow & R. Barkow eds., 2011) (discussing corporate civil liability).

The extensive literature on public enforcement of the securities laws against organizations includes: Steven Choi and Adam C. Pritchard, *SEC Investigations and Securities Class Actions: An Empirical Comparison*, 13 *J. EMPIRICAL LEGAL STUD.* 27 (2016); Steven Choi and Adam C. Pritchard, *The SEC's Shift to Administrative Proceedings: An Empirical Assessment*, 34 YALE J. ON REG. 1 (2017); Steven Choi and Adam C. Pritchard, *Securities Law and Its Enforcers, in* RESEARCH HANDBOOK ON CORPORATE CRIME AND FINANCIAL MISDEALING 219 (Jennifer Arlen, ed., 2018); James Cox & Randall Thomas, *Public and Private Enforcement of the Securities Laws: Have Things Changed Since Enron?*, 80 Notre Dame L. Rev. 893 (2005); Michael Klausner & Jason Hegland, *Corporate and Individual Liability in SEC Enforcement Actions*, RESEARCH HANDBOOK ON CORPORATE CRIME AND FINANCIAL MISDEALING (Jennifer Arlen ed., 2018); Urška Velikonja, *Politics in Securities Enforcement,* 50 GA. L. REV. 17 (2015); Urška Velikonja, *Public Enforcement After* Kokesh*: Evidence from SEC Actions*, 108 GEO. L.J. 389 (2019). See also Jennifer Arlen & William Carney, *Vicarious Liability for Fraud on Securities Markets: Theory and Evidence*, 1992 U. ILL. L. REV. 691 (1992); Anat Carmy Wiechman, Steven Choi and Adam C. Pritchard, *Scandal Enforcement at the SEC: The Arc of the Option Backdating Investigations*, 15 AM. L. & ECON. REV. 542 (2013).

The extensive literature on environment enforcement includes: Eric Helland, *Prosecutorial Discretion at the EPA: Some Evidence on Litigation Strategy*, 19 J. REG. ECON. 271 (2001); Eric Helland, The Enforcement of Pollution Control Laws: Inspections, Violations and Self-reporting, 80 Rev. Econ. Stat. 141 (1998); Eric Helland, *The Revealed Preferences of a State EPA: Stringency, Enforcement and Substitution*, J. ENV'T. ECON. & MGMT. 242 (1998).

§ 6.25. Policies Governing Admissions of Facts and Denials of Culpability

(a) An organization that engaged in knowing or intentional material misconduct should presumptively be offered a nontrial resolution that formally adjudicates the organization's culpability or require the organization to fully admit to the facts underlying the misconduct unless:

(1) the organization meets the requirements for a nontrial resolution that avoids triggering collateral consequences under § 6.24(b);

(2) such a determination or admission would trigger mandatory, presumptive, or permissive collateral consequences and § 6.24(c) is satisfied; or

(3) the following conditions are met:

(A) the organization fully remediated in accordance with § 6.07;

(B) the organization provided substantial material cooperation to enforcement officials that either enabled them to either detect and terminate misconduct more rapidly than they could have on their own or provided them with evidence material to their case(s) against the individuals responsible for the misconduct that they could not reasonably have obtained on their own in a timely way; and

(C) a finding of culpability or a full admission could subject the organization to substantial penalties or liability imposed by other parties that cannot be addressed through a coordinated resolution with those parties.

(b) Except as provided in subsection (c), nontrial resolutions that do not adjudicate the organization's culpability or require a full admission of the facts of the misconduct should:

(1) require the organization to admit to most of the material facts of the misconduct; and

(2) state that the organization cannot deny its culpability for the misconduct except in litigation brought against it by others who are not parties to the nontrial resolution.

(c) Civil and administrative enforcement officials entering into a nontrial resolution that does not involve a finding of culpability or a full admission of the facts needed to

establish the alleged misconduct should not preclude the organization from denying its culpability for the misconduct if, at the time of the resolution:

(1) the organization provided full cooperation in accordance with § 6.05;

(2) enforcement officials lack sufficient evidence to establish the organization's culpability for the alleged misconduct and do not expect to be able to obtain the evidence needed to prove the misconduct without incurring costs that are excessive relative to the benefit to the public that an admission would provide;

(3) enforcement officials have good-faith and reasonable belief that they could obtain the necessary evidence if they incurred the necessary cost; and

(4) the nontrial resolution sets forth the reasons why the enforcement authority is agreeing to a denial-permitted resolution with the organization.

Comment:

a. Relationship to Section 6.24. Section 6.24 provides guidance on when civil or administrative enforcement officials should resolve a case through a nontrial resolution that would not trigger collateral consequences. Section 6.25 provides guidance on when enforcement officials should enter into a non-trial resolution that does not adjudicate the organization's culpability or require it to admit to the full facts of the misconduct. Such admissions may be material to the organization because of they could result in the imposition of collateral consequences. The considerations that support a no-collateral consequences resolution thus also support nontrial resolutions that do not require full admissions in such circumstances. Yet admissions can be material to the organization for other reasons, including the threat of liability to third parties. This Section offers guidance on the policies to govern no-admission or partial-admission resolutions when the ability to avoid a full admission provides a material benefit to the organization that can be used as an incentive for it to self-report, fully cooperate, and remediate.

b. External consequences of either a determination of the organization's culpability or a full admission of the underlying facts. A nontrial resolution that formally adjudicates an organization's culpability or requires the organization to admit to all of the facts of its misconduct could cause the organization to incur substantial and unpredictable additional costs if other actors, including other enforcement authorities, use the finding or admission to establish the organization's culpability and liability in a separate action. The potential downstream effects of such a nontrial resolution could deter organizations from self-reporting misconduct or fully

cooperating and thereby undermine enforcement efforts. This, in turn, may result in misconduct remaining undetected and unremediated and individual wrongdoers escaping justice.

Civil or administrative enforcement officials with jurisdiction over situations in which the threat of follow-on third party litigation is likely to deter organizations from self-reporting or fully cooperating if they are required to admit to the full facts of this misconduct should adopt a presumption that organizations that undertake full corrective action or cooperate in accordance with § 6.25(a) can enter into a nontrial resolution that does not either involve a formal finding of culpability or require the organization to admit to all the facts of the misconduct. By including provisions in such nontrial resolutions that require disgorgement, restitution, and remediation in accordance with § 6.07, civil and administrative enforcement officials often can ensure that victims' harms are redressed.

c. Culpability resolutions and full admissions. Enforcement authorities should adopt a presumption favoring nontrial resolutions that require an organization to admit to the facts of its knowing or intentional material misconduct when the admission would not trigger collateral consequences or present the organization with an enhanced material risk of liability to third-parties.

Several important goals of civil and administrative enforcement are served when enforcement authorities require organizations to admit to their wrongdoing. Such an admission unambiguously establishes —for the public, the organization's employees, and the organization's current and future counterparties—that it engaged in misconduct. It promotes the law's ability to identify and appropriately blame those who engaged in misconduct. It also promotes the goals of deterrence and, in some cases, public safety, by providing third parties with information that may be material to their decisions whether to engage in future dealing with the organization.

Enforcement authorities should not require enforcement officials to require a full admission when they do not have sufficient evidence to establish an organization's culpability under the requisite legal standard, however.

d. Considerations justifying a partial-admission or no-admission resolution. Enforcement authorities should adopt a policy of offering an organization a no-culpability, partial-admission resolution when:

(1) the organization meets the requirements for a nontrial resolution that avoids triggering collateral consequences under § 6.24(b);

(2) the organization's actions enabled enforcement officials to either detect and terminate misconduct more rapidly than they could have on their own or provided enforcement officials with evidence material to their investigation that they could not reasonably have obtained on their own in a timely way; and

(3) a culpability determination by the agency or full admission to the underlying facts of the misconduct could be used by other parties, such as other government authorities or private parties, to establish the organization's liability to those other parties.

Partial or no-admission resolution are justified under these circumstances by the benefit to the public of providing strong incentives for organizations to self-report and cooperate. Self-reporting and cooperation in these circumstances should help to deter misconduct by making detection and enforcement more likely, terminate and remediate existing misconduct more rapidly, promote rehabilitation of the organization, provide faster restitution to victims, and help ensure that individual wrongdoers are brought to justice. They should not be granted in other situations.

e. Considerations that do not justify a partial-admission or no-admission resolution. Enforcement authorities should adopt a presumption against resolving enforcement actions involving knowing or intentional material misconduct through partial- or no-admissions resolutions in situations in which the organization has not provided the level of cooperation needed to satisfy § 6.24(b). The desire to expedite the enforcement action or to avoid the delay and risk of going to trial are generally not adequate reasons to offer an organization a no-admission nontrial resolution, except as provided in § 6.25(c). To offer organizations no-admission nontrial resolutions on these bases alone would undermine enforcement officials' ability to structure enforcement policy to induce organizations to self-report, fully cooperate, and remediate. Organizations would have substantially weaker incentives to self-report, fully cooperate, or fully remediate if they have good reason to believe that enforcement officials are likely to offer them a partial-admission or no-admission resolution even when they fail to take such corrective actions but agree to settle expeditiously. Favoring expeditious resolution of an individual case at the expense of creating strong incentives for organizations to self-report and fully cooperate would undermine enforcement officials' ability to detect misconduct, to more expeditiously determine the full scope of any misconduct, and to identify and obtain the information necessary to pursue enforcement actions against the individuals who knowingly or intentionally committed material misconduct. The temptation to obtain a speedy resolution in a specific individual case is unlikely

to be worth the negative impact of signaling to organizations that they need not satisfy § 6.25(a) if they are willing to enter into a speedy no-admission resolution.

In addition, allowing organizations to obtain no-admission resolutions without cooperating in order to speed the process in effect rewards organizations that help create problems of proof by refusing to fully cooperate. A policy of presumptively taking organizations to court if they do not fully cooperate serves the interests of justice by providing strong incentives for organizations to fully cooperate, even if the policy delays resolution of those cases in which organizations do refuse to cooperate.

Enforcement authorities can better address the twin challenges of obtaining the needed evidence and motivating organization to cooperate by adopting enforcement policies—and, when applicable, regulations—that enhance their access to evidence. Such policies include those that favor:

(1) using cooperation agreements with individuals who are implicated in the misconduct but who are not primarily responsible for it and are subordinate to other individuals implicated in the misconduct;

(2) using data analytics to detect misconduct and identify wrongdoers;

(3) using investigators trained to investigate the misconduct in question; and

(4) adopting (or taking actions to urge legislatures to adopt) effective whistleblower bounty provisions designed to give adequate compensation and protections against retaliation to whistleblowers who provide enforcement authorities with material evidence of misconduct.

f. Importance of obtaining evidence against and pursing enforcement actions against individuals that engage in knowing or intentional material misconduct. An organization should not be permitted to obtain a partial- or no-admission resolution for misconduct involving knowing or intentional material misconduct by individuals unless the organization provides the government with all material information that is reasonably available to it about the responsible individuals' role in the misconduct. Enforcement officials should pursue civil or regulatory enforcement actions against individuals who knowingly or intentionally committed material misconduct that warrants enforcement, even if the individuals do not have sufficient assets to pay substantial monetary sanctions. Enforcement is needed to deter misconduct. A monetary sanction that is large relative to the individual's available assets can have a powerful deterrent effect on the individuals who are

responsible for the misconduct. Enforcement officials can also deter misconduct by imposing collateral sanctions on individuals with a history of misconduct who present a heightened risk of future misconduct. Individual enforcement actions also provide a strong statement to the public—that should reverberate within the organization—that the individuals' actions were unlawful and sufficiently serious to warrant enforcement.

g. Presumption favoring no-denial resolutions. An enforcement official entering into a partial-admission or no-admission resolution should presumptively structure the nontrial resolution as a no-denial resolution if he or she have, or reasonably and in good faith believe he or she could obtain, sufficient evidence to establish the organization's culpability. A provision that precludes an organization from denying the misconduct in public should nevertheless allow the organization to deny the misconduct in any legal action brought by a third party unless the nontrial resolution adjudicated the organization's culpability or required it to fully admit to all the facts of the misconduct. But the organization should not be allowed to deny the misconduct in statements to its employees or to the public.

The presumption against denial-permitted enforcement actions arises from two considerations. First, the public has a strong interest in having a clear statement about whether the organization engaged in misconduct. Second, the organization's public acceptance of responsibility for its knowing or intentional misconduct should facilitate its efforts to address the internal root causes of the misconduct. An organization that denies that its actions constituted misconduct is unlikely to be able to convince its employees that ethics and the law require that they avoid such conduct in the future.

The presumption that an organization should not be permitted to deny its misconduct rests on the assumption that enforcement officials are acting appropriately in requiring the organization to accept responsibility for misconduct. Thus, enforcement officials should have, or expect to be able to obtain, sufficient evidence to make a strong prima facie case against the organization that would support a finding that the organization is liable.

h. Denial-permitted resolutions. Section 6.25(c) recognizes that a denial-permitted resolution are appropriate in the rare circumstances in which:

(1) enforcement officials have a sufficient factual and evidentiary basis for believing that an organization engaged in knowing or intentional material misconduct;

(2) the organization fully cooperated;

(3) enforcement officials do not currently have sufficient evidence to establish the organization's culpability; and

(4) enforcement officials believe that they would need to spend excessive resources to conduct a full investigation in order to obtain that evidence.

When enforcement officials enter into a nontrial resolution with an organization without having sufficient evidence to prove that the organization committed the alleged misconduct, they should permit the organization to deny its misconduct even when the organization is settling because it expects they will be able to obtain such evidence. By contrast, given the public's strong interest in knowing whether an organization engaged in material misconduct, organizations should not be permitted to publicly deny (outside of the context of litigation) any knowing or material misconduct that enforcement officials have sufficient evidence to establish.

Organizations should not be allowed to deny misconduct if the organization helped contribute to enforcement officials' inability to prove the misconduct by failing to cooperate. Thus, this Section establishes that enforcement officials should permit an organization to deny its misconduct only when it has fully cooperated. This limitation addresses the concern that organizations would otherwise be tempted to delay cooperation in the hope of undermining the government's ability to prove its case while simultaneously obtaining a partial-admission, denial permitted resolution by satisfying § 6.25(b). To deter organizations from providing only partial cooperation, enforcement authorities should adopt a policy of proactively targeting their investigative resources at organizations that engaged in knowing or intentional material misconduct and refused to fully cooperate.

Enforcement officials also should not use denial-permitted resolutions in situations in which they do not have, and do not reasonably expect to be able to obtain, the evidence needed to sanction organizations. Rather, in such situations, enforcement officials should not pursue an enforcement action.

REPORTERS' NOTES

a. Admissions. For a discussion of resolutions with full admissions, partial admissions, and no admissions, see the Reporters Notes following § 6.21. For a discussion of the importance of providing the public with a full picture of the nature of an organization's misconduct and its culpability for it, see § 6.02, Comments *b-d*.

b. Denials following an enforcement authority's determination that the organization engaged in misconduct. No-admission resolutions are regularly predicated on an official

determination by the relevant enforcement authority that the organization engaged in the misconduct. In order to promote public confidence in such determinations, enforcement authorities should only make a finding that an organization violated the law if there is sufficient evidence to establish each element needed to prove the violation under the relevant standard of proof. When there is sufficient evidence, it is difficult to justify allowing an organization to deny its culpability because a denial would undermine both the faith of both the public and the organization's own employees in the legitimacy of the enforcement authority's actions. Thus, when an organization refuses to provide adequate cooperation, enforcement authorities may need to incur the costs needed to establish its culpability, even in circumstances in which the resources required to do so appear to be excessive given the magnitude of the violation.

Enforcement authorities need to pursue enforcement actions against organizations that committed material misconduct and refused to cooperate in order to promote deterrence (specific and general). Enforcement authorities can promote public confidence in their other enforcement actions by reserving an organization's ability to deny culpability for circumstances in which enforcement officials conclude that the costs of pursuing an investigation sufficient to establish the organization's liability are excessive. This policy would offer the important benefit of deterring enforcement officials from making too ready use of "denial-permitted" resolutions in order to expedite resolving cases in order to be able to report a high number of resolved cases. If the policy were implemented, a "denial-permitted" resolution would indicate that enforcement officials had not yet obtained sufficient evidence to establish that the organization committed the misconduct.

c. Enforcement losses. Achieving the goal of promoting admissions and limiting denials in cases involving knowing and intentional misconduct will likely require enforcement authorities to pursue litigation in cases that otherwise might have been resolved through no-admission and denial-permitted nontrial resolutions. Enforcement officials will lose some of these actions. Legislatures and other oversight authorities can promote the goals of these Principles by refraining from expressing public disapproval of enforcement authorities that lose a case absent evidence that establishes beyond a reasonable doubt that either enforcement officials did not have a good-faith reasonable basis for bringing the enforcement action or were grossly negligent in handling the case.

§ 6.26. Collateral Consequences: Debarment, Exclusion, and Delicensing

To the extent permitted by applicable laws, the following Principles set forth the most effective use of a government agency's authority to impose collateral consequences on an organization under the agency's jurisdiction.

(a) Collateral consequences, such as debarment, exclusion, and delicensing for knowing or intentional material misconduct, should be reserved for situations in

which the agency has established that an organization engaged in the misconduct and concluded that:

(1) the organization continues to present a significant risk of committing future material violations that pose harm to the interests that the agency is charged with protecting; and

(2) the risk of future violations cannot be adequately addressed through other means, such as mandated internal reforms, enhanced oversight, or the appointment of a compliance monitor in accordance with §§ 6.09–6.12.

(b) Government officials with authority to impose collateral consequences on an organization that engaged in misconduct presumptively should not impose them on organizations that satisfied § 6.24(b).

(c) Evidence that an organization committed a violation generally does not, in and of itself, establish that the organization presents a significant risk of committing future misconduct when the organization's liability is predicated on either respondeat superior or on absolute liability imposed by a public welfare statute.

(d) In determining whether an organization continues to present a significant risk of committing future material violations sufficient to justify imposing collateral consequences on it, officials should consider the following factors:

(1) whether the misconduct was committed or condoned by high-level personnel in the organization or a unit thereof who remain in positions of authority;

(2) whether the misconduct was widespread within a unit of the organization or across multiple units of the organization and was committed or knowingly condoned by high-level or substantial authority personnel who remain in positions of authority;

(3) whether the misconduct conferred benefits on the organization that were sufficiently large to potentially motivate the organization to engage in similar misconduct in the future, and the risk of this misconduct cannot be adequately reduced through measures such as appointing a compliance monitor;

(4) whether the organization's compensation, promotion, retention, or disciplinary policies were a substantial cause of the misconduct and whether the organization has fully remediated them;

(5) whether the organization has fully remediated all of the deficiencies in its compliance function that existed at the time of the misconduct; and

(6) whether the organization has fully demonstrated its commitment to preventing and deterring misconduct by providing all information reasonably available to it regarding the scope of the misconduct and the identity of, and evidence against, those individuals responsible for it.

(e) Collateral consequences should be restricted to the specific business unit or units within the organization that committed the misconduct and continue to present an ongoing risk, whenever applicable laws allow the authorities to do so. The collateral consequences should remain in place for the period of time necessary for the organization to remediate the internal root causes of the misconduct.

(f) When an organization does not present a substantial risk of committing the same offense in the future, it may be appropriate for those officials with authority over whether to impose collateral consequences to inform both the organization and any other enforcement officials with the authority to sanction the organization that the organization will not be subject to collateral consequences should it be sanctioned for the detected misconduct, if such a waiver is allowed under applicable law.

Comment:

a. Purpose of collateral consequences. Collateral consequences should not be used as a form of retribution against organizations that have engaged in material misconduct. They should be used only to protect the relevant agency, or those that it is authorized to protect, from the risk of future harm that could result from future dealings with an organization that the agency has determined presents a significant risk of future material misconduct.

An organization that engaged in knowing or intentional material misconduct should not be automatically deemed to present a significant risk of future material misconduct. This statement applies even when the organization has been found to have engaged in fraud or other misconduct involving moral turpitude. When a natural person is accused of fraud, it can reasonably be demonstrated that person possessed the necessary mental state for the offense. But, under U.S.

law, a large multinational organization can be found to have engaged in fraud if a single, low-level employee at one of its locations committed fraud in the scope of his or her employment, notwithstanding the organization's good faith, genuine, and active commitment to preventing, deterring, and detecting fraud and punishing those responsible. In such circumstances, the culpability of the employee does not indicate that the organization itself is willing to commit misconduct in pursuit of gain.

Thus, while that the violation of certain laws or regulations, or the imposition of certain forms of relief for violations of the law or regulations, can trigger collateral consequences, authorities charged with imposing collateral consequences should, to the extent consistent with applicable law, look beyond the violation to assess whether the facts of the misconduct and the organization's response to it support the conclusion that the organization presents a significant risk of future material misconduct that cannot be better addressed through other means that are less costly to society, such as mandated internal reforms, enhanced oversight, or the appointment of a monitor.

b. Preconditions for imposing collateral sanctions. To the extent permitted by applicable laws, a government agency should create a presumption against imposing collateral consequences on an organization unless:

(1) both the facts of the misconduct and the organization's response to it provide a reasonable basis for concluding that the organization presents a significant risk of future material misconduct that could cause substantial harm to the agency or those it is charged with protecting; and

(2) the risk of future violations cannot be adequately addressed through other means, such as mandated reforms imposed in accordance with § 6.09, enhanced oversight by a regulatory authority, or a monitor imposed in accordance with §§ 6.10–6.12.

c. Factors that supporting imposing collateral consequences. Enforcement authorities should assess certain factors when determining whether the organization presents a significant risk of future material misconduct.

First, government authorities should assess whether the misconduct was isolated or appears to have arisen out of deeper problems with the organization's culture and/or compliance program. One important factor for determining whether the organization was plagued by fundamental compliance problems at the time of the misconduct is whether the organization failed to have an

effective compliance program in place at the time of the misconduct. Additional factors that indicate that the organization was plagued by fundamental problems at the time of the misconduct include that:

(1) the misconduct was committed or condoned by high-level personnel of the organization or a unit of the organization;

(2) the misconduct was widespread within a unit of the organization or across multiple units of the organization; or

(3) the misconduct conferred substantial benefits on the organization and the organization could repeat the misconduct.

Second, government authorities should assess whether the organization has presently demonstrated a genuine commitment to ensuring its future compliance with the law. The pertinent question is whether the organization has taken all the steps that should be expected of an organization that engaged in knowing and intentional misconduct and is committed to ensuring that its employees know that such conduct should not reoccur. Specifically, enforcement officials should look to see whether the organization fully demonstrated its commitment to preventing and deterring misconduct by:

(1) providing all information reasonably available on the scope of the misconduct and the identity of, and evidence against, those responsible for it;

(2) acting reasonably and in good faith to implement an effective compliance program in accordance with § 6.08; and

(3) acting reasonably and in good faith to fully remediate the root causes of the misconduct in accordance with § 6.07, including by ensuring that any high-level or substantial authority personnel who committed, knowingly condoned, or detected and knowingly failed to act in good faith to terminate the misconduct no longer hold positions of authority at the organization.

Enforcement officials may reasonably infer that organizations that have not taken these actions or took them reluctantly and with considerable delay are unlikely to be effective at undertaking the reforms needed to transform the pre-existing internal culture of the organization into a culture that is effective at ensuring that employees comply with the law.

d. Mandated reforms, disciplinary actions, enhanced oversight by regulatory authorities and compliance monitors as alternatives to collateral consequences. To the extent that an agency

has discretion to waive collateral consequences, government officials with authority to impose collateral consequences should assess whether the significant risk of an organization engaging in future material misconduct can be effectively addressed through a combination of mandated reforms of the organization's compliance function, in accordance with § 6.08; appropriate disciplinary action involving those responsible for committing or knowingly condoning misconduct, in accordance with § 6.07; additional oversight or auditing by the regulator; and/or the appointment of a compliance monitor, in accordance with § 6.10-6.12. These approaches to ensuring the organization's future compliance with the law generally are superior to collateral consequences such as debarment, exclusion, or delicensing because they are directly aimed at ensuring the organization's compliance and place the costs of achieving compliance squarely on the organization with relatively little collateral damage to consumers, suppliers, and employees in units that had no role in the misconduct.

e. Targeted collateral consequences. To the extent that the agency imposing collateral consequences has authority over their scope, it should restrict collateral consequences such as debarment, exclusion, and delicensing to the specific business unit or units within the organization that engaged in the misconduct and continue to present an ongoing risk. These consequences should be imposed until the organization has fully remediated the root causes of the misconduct.

A policy of targeting collateral consequences at those units that were both involved in the misconduct and continue to present a risk of future misconduct—instead of imposing them on the entire organization—promotes the goals of prevention, deterrence, rehabilitation, and ensuring that restitution is provided to victims in a variety of ways. The policy promotes those goals by enabling enforcement authorities to target collateral consequences at those units within an organization that were both responsible for the misconduct and have not fully remediated the root causes of the misconduct, without imposing unjustified hardship on customers, suppliers, and employees of units that had no involvement in the misconduct and do not present a significant risk of future material misconduct.

This policy also helps ensure that restitution it provided to victims. Organization-wide debarment can undermine that goal if it leads the organization to declare bankruptcy. By targeting collateral consequences at the unit(s) that present an enhanced risk of harm, enforcement officials leave the rest of the organization free to generate the profits that may be needed to provide funds to compensate victims for their losses.

While targeted collateral consequences are generally preferable to organizational-wide collateral consequences, when enforcement officials enter into an enforcement resolution with an organization whose executive management or controlling shareholders participated in or knowingly condoned the misconduct, they should predicate any offer to impose targeted—as opposed to organization-wide—collateral consequences on the organization demonstrating that the executives or controlling shareholders who were responsible for the misconduct are no longer in positions to influence the organization.

REPORTERS' NOTES

a. Potentially perverse effects of collateral consequences. Legislatures and administrative agencies regularly adopt statutes or regulations, respectively, that provide that certain forms of misconduct can result in an organization being precluded from: (1) providing goods or services to the agency or the customers it serves: or (2) having access to certain markets or otherwise being disadvantaged in a market. There are good reasons to impose such consequences when they serve to protect the public. But many statutes and regulations both:

(1) set forth conditions for triggering mandatory or presumptive collateral consequences that result in the imposition of collateral consequences n a great many situations in which they are not appropriate; and

(2) do not provide an effective mechanism for obtaining a waiver of such consequences that would enable a criminal or civil enforcement official negotiating a nontrial resolution for organizational misconduct to readily obtain a waiver of the collateral consequences at the time of resolution is being negotiated, when a waiver would be appropriate.

As a result, laws providing for collateral consequences can have the perverse effect of undermining deterrence in the very situations in which it is most needed if criminal and civil enforcement officials feel compelled to eschew full and appropriate enforcement against an organization that engaged in material misconduct because of the cost to society of the collateral consequences that would be triggered by their actions.

Criminal, civil, and administrative enforcement officials are justifiably loath to enter into a nontrial resolution, such as a guilty plea, with a publicly held corporation that would trigger collateral consequences because they are concerned that customers and others could lose access to needed goods or services, such as prescription drugs.

The problem of perverse effects is particularly great with laws that provide for mandatory debarment of an entire organization if any unit of it is found to have committed certain forms of misconduct. But it also can arise when certain enforcement actions presumptively trigger a material collateral consequence imposed on the entire organization and the procedure for determining whether the collateral consequence is imposed or waived is such that the waiver

decision cannot practicably be made at the time that the nontrial resolution for the material misconduct is negotiated.

This perverse effect can undermine the effectiveness of enforcement. Responding to the threat of collateral consequences, prosecutors have offered deferred prosecution agreements (DPAs) to organizations that did not fully cooperate because they were the leading providers of certain medical devices. Of course, this creates the risk that organizations that make vital goods and services will not feel compelled to self-report or fully cooperate because they are confident of obtaining a DPA without engaging in full cooperation because of the cost to society of convicting them.

Laws providing for collateral consequences also can distort enforcement outcomes. For example, concern for about the adverse consequences of imposing collateral consequences on an entire organization has led prosecutors to enter into agreements under which a subsidiary of the organization pleads guilty and is debarred, even though it was not genuinely implicated in the organization's misconduct, in order to target the collateral consequences at an entity that does not provide important goods or services to the public. For a discussion of these issues see Cindy R. Alexander & Jennifer Arlen, *Does Conviction Matter? The Reputational and Collateral Effects of Corporate Crime*, Section 5, *in* RESEARCH HANDBOOK ON CORPORATE CRIME AND FINANCIAL MISDEALING (Jennifer Arlen ed. 2018).

b. Collateral consequences of material violations of the securities laws. An organization convicted of violating the securities laws or found liable in a civil or administrative action may face a variety of collateral consequences. These include:

(1) loss of well-known seasoned issuer (WKSI) status for the purposes of securities offerings;

(2) disqualification under Section 9(a) of the Investment Company Act of 1940 (1940 Act);

(3) loss of private-offering exemptions provided by Regulations A and D under the Securities Act of 1933 (Securities Act);

(4) loss of the exemption from registration under the Securities Act for securities issued by certain small business investment companies and business development companies provided by Regulation E; and

(5) a prohibition barring a registered investment adviser from receiving cash fees for solicitation under Rule 206(4)-3 of the Investment Advisers Act of 1940 (Advisers Act).

See generally Richard A. Rosen & David S. Hunington, *Waivers from the Automatic Disqualification Provisions of the Federal Securities Law*, 29 INSIGHTS 2 (Aug. 2015). The Securities and Exchange Commission (SEC) can waive disqualifications, usually upon a showing of "good cause." Id.

An organization can face disqualification in a variety of circumstances involving less culpability than a finding that the organization engaged in intentional securities fraud. For example, under Rule 405 of the Securities Act, an issuer that is the subject of an administrative

order that either determines that it violated the antifraud provisions of the federal securities laws or that prohibits a future violation of such laws can be rendered ineligible for WKSI status. This can result from violations for misconduct that did not involve scienter because Sections 17(a)(2) and 17(a)(3) of the Securities Act and Sections 206(2) and 206(4) of the Advisers Act are non-scienter-based antifraud provisions. Disqualification applies to a dually registered company and any parent public issuer.

Broker-dealers and investment advisers may be disqualified from participating in either Rule 506 offerings or offerings under other offering exemptions (Rule 504, Regulation A, Regulation CF) as, among other things, an issuer, beneficial owner, investment manager, underwriter, or compensated solicitor, or in Reg E transactions as, among other things, an issuer, beneficial owner, underwriter, or compensated solicitor by, respectively:

(1) the SEC's entry of a cease-and-desist order that will include "ordered" undertakings or other limitations on activities or functions (e.g., multistep remedial measures); or

(2) an SEC order entered pursuant to the Securities Exchange Act of 1934 (Exchange Act) § 15(b) and Advisers Act § 203(e) with ongoing sanctions (i.e., action to still be completed).

In addition, companies found to have violated the antifraud provisions of the securities laws may be more vulnerable to private litigation, both through the operation of offensive collateral estoppel and as a result of the loss of an important safe harbor. Both the Securities Act and the Exchange Act offer companies a safe harbor for certain forward-looking statements. Private Securities Litigation Reform Act of 1995, 15 U.S.C. § 78u-5. A company is not eligible for the safe harbor if it was:

(1) was convicted of a felony or certain misdemeanors; or

(2) was made the subject of a judicial or administrative decree or order arising out of a governmental action that:

(a) determines that the issuer violated;

(b) requires that the issuer cease and desist from violating; or

(c) prohibits future violations of; the antifraud provisions of the securities laws. 15 U.S.C. § 78u-5(b).

c. Federal debarment for FCPA violations. Federal regulations governing procurement provide that an individual or company that violates the Foreign Corrupt Practices Act or other criminal statutes can be barred from doing business with the federal government. The Federal Acquisition Regulations governing the use of debarment make clear that debarment should not be used as a punishment. It is intended to be used only if "in the public's interest for the Government's protection." Debarment is intended to be used when the government concludes that the facts and circumstances of the misconduct and subsequent events provide sufficiently strong indicia that the organization lacks business integrity or honesty to "seriously and directly affect[] the present responsibility of a Government contractor or subcontractor." 48 C.F.R. § 9.402(b); see generally

CRIMINAL DIV., U.S. DEPT. OF JUSTICE; ENF'T DIV., SEC. & EXCH. COMM'N, FCPA: A RESOURCE GUIDE TO THE U.S. FOREIGN CORRUPT PRACTICES ACT 72-73 (2d. ed. 2020) https://www.justice.gov/criminal-fraud/file/1292051/download.

Federal procurement regulations set forth a list of factors to consider. Consistent with the approach of this Section—and with the approach taken to monitors in §§ 6.19 & 6.20—the regulations take into account, as factors weighing against debarment:

> (1) whether the organization had effective standards of conduct and internal control systems in place at the time of the activity that constitutes a cause for debarment;
> (2) whether the organization remediated and adopted effective procedures prior to any government investigation of the activity cited as a cause for debarment;
> (3) whether the organization engaged in timely self-reporting;
> (4) whether the organization fully investigated the misconduct and, if so, fully cooperated with enforcement authorities and with the debarring officials; and
> (5) whether the organization fully remediated, including remediying the problems that gave rise to the misconduct and taking appropriate disciplinary action against the individuals responsible for the misconduct.

See 48 C.F.R. § 9.406–1.

d. Federal debarment and exclusion of organizations found liable for health-care fraud. Pursuant to its governing statute, the Department of Health and Human Services (HHS) can exclude an organization from engaging in business with the agency—including, but not limited to, seeking reimbursement for services provided to Medicare and Medicaid patients—if the organization had been found liable for committing a variety of offenses. The predicate offenses that can trigger mandatory or presumptive exclusion include misconduct aimed directly at the agency (such as filing a false claim with the agency) and offenses that are within the agency's direct enforcement authority. The types of misconduct potentially triggering exclusion include: submitting claims for excessive charges or unnecessary services; engaging in fraud, kickbacks, or other prohibited activities; knowingly making or causing to be made certain types of false statements; and a range of other offenses that bear on the entities' suitability as either a government counterparty or a provider of services to patients. In addition, some other forms of fraud (such as false claims against other agencies) may trigger permissive exclusion, but only under certain circumstances, discussed below. See Social Security Act, 42 U.S.C. § 1320a-7(a)(3) & (4).

A firm that engaged in misconduct of the type described above can be excluded if the firm was convicted of the offense or the organization was found to have engaged in the misconduct in a civil-enforcement action or in an administrative proceeding of the agency. Id. Some determinations result in mandatory exclusion (see Reporters' Note *d*), and others result in permissive exclusion.

The Social Security Act allows permissive exclusion if the firm was convicted "(B) of a criminal offense relating to fraud, theft, embezzlement, breach of fiduciary responsibility, or other financial misconduct with respect to any act or omission in a program (other than a health care

program) operated by or financed in whole or in part by any Federal, State, or local government agency." Social Security Act Section 1128B(f), 42 U.S.C. § 1320a-7. The Social Security Act also provides for permissive exclusion if the agency determines that an organization committed health-care fraud or crimes relating to controlled substances, whereas HHS's own determination that the firm committed these offenses triggers mandatory exclusion. 42 U.S.C. § 1320a-7(a)(3) & (4).

In determining whether to exercise its permissive-exclusion authority, HHS, like many other federal agencies, assesses whether the organization presents a future risk to the interests it is authorized to protect—here federal health-care programs. Of particular importance, the agency has determined that exclusion "often" is not necessary if any risk of future misconduct can be effectively ameliorated by "appropriate integrity obligations," such as voluntary reforms undertaken by the organization, mandatory reforms imposed by the agency through a corporate-integrity agreement, or through the appointment of a monitor. See Criteria for Implementing Section 1128(b)(7) Off. of Inspector Gen., U.S. Dept. of Health & Human Servs., Criteria for implementing section 1128(b)(7) exclusion authority (April 18, 2016), https://oig.hhs.gov/exclusions/files/1128b7exclusion-criteria.pdf. For a discussion of mandatory compliance program reforms, see § 6.09; for a discussion of monitors, see §§ 6.10–6.12.

By contrast, the Social Security Act provides that an organization that was convicted of a felony relating to health-care fraud or crimes relating to controlled substances is subject to mandatory exclusion. 42 U.S.C. § 1320a-7(a)(3) & (4). The law also substantially restricts the agency's ability to waive mandatory exclusion. The agency can only exempt an organization from exclusion if it determines that: (1) the organization is the sole source of an "essential service in a community"; (2) exclusion would impose a hardship on the beneficiaries; and (3) exclusion would not be in the public interest. 42 C.F.R. § 1001.1801. The agency's authority to waive is restricted to the program and the service for which the organization is the "sole source." Thus, under these provisions, a convicted firm could end up excluded from selling most of its products to Medicaid beneficiaries, even if it is granted a waiver with respect to some of them. As a result, conviction can force the agency to exclude a firm that it otherwise would not want to exclude.

e. Mandated reforms as an alternative to debarment. The availability of mandated reforms, including appointment of a monitor, also appear to weigh against debarment. For example, the Department of Health and Human Services often imposes its own oversight requirements, such as corporate-integrity agreements, to provide adequate assurance that the organization will comply with its legal requirements, thereby obviating the need for exclusion. See generally CRIMINAL DIV., U.S. DEPT. OF JUSTICE; ENF'T DIV., SEC. & EXCH. COMM'N, FCPA: A RESOURCE GUIDE TO THE U.S. FOREIGN CORRUPT PRACTICES ACT 72-73 (2d. ed. 2020).

f. Individuals and collateral consequences. A variety of federal agencies have authority to bar individuals who have engaged in certain types of misconduct from either serving as officers or directors of organizations under the agency's jurisdiction or appearing before the agency.

For example, an individual found to have violated the antifraud provisions of the securities laws may be temporarily or permanently barred by either a court or the SEC from serving as an officer or director of a public company under certain circumstances. Securities Enforcement

Remedies and Penny Stock Reform Act of 1990, 15 U.S.C. §§ 77t(e) & 78u(d)(2); Sarbanes-Oxley Act of 2002, amending § 20(e) of the Securities Act and § 21(d)(2) of the Exchange Act.

Rule 102(e) of the SEC's Rules of Practice provide that the SEC may permanently or temporarily deny the privilege of appearing or practicing before it in any way to an attorney or accountant under certain circumstances. One finding sufficient to justify a bar is that the person was found "to have willfully violated, or willfully aided and abetted the violation of any provision of the Federal securities laws, or the rules and regulations thereunder."

g. Academic literature. Scholarly discussion of collateral consequences include Cindy R. Alexander & Jennifer Arlen, *Does Conviction Matter? The Reputational and Collateral Effects of Corporate Crime*, Section 5, *in* RESEARCH HANDBOOK ON CORPORATE CRIME AND FINANCIAL MISDEALING (Jennifer Arlen ed. 2018); Erling Hjelmeng & Tina Søreide, *Debarment in Public Procurement: Rationales and Realization*, *in* INTEGRITY AND EFFICIENCY IN SUSTAINABLE PUBLIC CONTRACTS (G.M. Racca & C. Yukins eds., 2014); Urška Velikonja, *Waiving Disqualification: When Do Securities Violators Receive a Reprieve?,* 103 CALIF. L. REV. 1081 (2015). For a discussion of collateral sanctions imposed by the World Bank, see STEFANO MANACORDA & COSTANINO GRASSO, FIGHTING FRAUD AND CORRUPTION AT THE WORLD BANK: A CRITICAL ANALYSIS OF THE SANCTIONS SYSTEM (2018); Sope Williams, *The Debarment of Corrupt Contractors from World Bank-Financed Contracts,* 36 PUB. CONT. L.J. 277 (2007).

§ 6.27. Protecting Employees and Agents Who Uphold the Law or Report Misconduct from Retaliation

(a) To the extent permitted by applicable law, civil and administrative enforcement authorities should adopt provisions that provide credible assurances that individuals who provide information about material misconduct to government authorities will not have their identity disclosed, directly or indirectly, until any whistleblower award has been paid, except when enforcement officials:

(1) need to identify the individual in the course of producing documents or calling witnesses during the course of a legal proceeding;

(2) receive authorization from the whistleblower to reveal the person's identity; or

(3) are ordered to reveal the person's identity by a court of law or a statute.

(b) To the extent allowed by law, civil and administrative authorities should protect whistleblowers from retaliation and pretaliation that is, or would be, based on their good-faith decision to report material misconduct internally or to the government.

(1) "Retaliation" includes termination, demotion, reduction of salary, and reduction of responsibilities and authority.

(2) "Pretaliation" is a preemptive effort by an employer to deter whistleblowing. An employer presumptively engages in pretaliation if it adopts any policy likely to be interpreted by a reasonable employee as restricting the employee's ability to disclose nonpublic information about misconduct within the organization to government authorities or self-regulatory bodies. Policies that potentially operate as pretaliation, absent a clause specifically stating that an employee retains the right to report suspected misconduct to the government or self-regulatory bodies and to obtain any recovery that might result from reporting, include:

(A) confidentiality and nondisclosure agreements;

(B) separation and severance agreements;

(C) nondisparagement agreements; and

(D) clauses establishing trade secret or other intellectual property rights in the organization's nonpublic information.

(c) To the extent allowed by law, civil and administrative authorities should adopt and enforce provisions that protect employees from retaliation or pretaliation if they object to conduct that they reasonably believe violates or would violate the law.

(d) An employer that acts adversely against an employee who reported misconduct or objected to engaging in misconduct should not be treated as having acted in retaliation if the employer:

(1) had taken material steps to take the adverse action against the employee prior to when:

(A) the employee decided to report the misconduct internally to the employee's superior or externally to the government;

(B) the organization anticipated that the employee was likely to report misconduct; and

(C) the employee objected to or the employer anticipated that the employee would object to conduct that the employee reasonably and in good faith believed violated the law; and

(2) the employee's decision or anticipated decision to report the misconduct internally or externally or to object to engaging in the misconduct was not a contributing cause of the employer's decision to act adversely against the employee.

Comment:

a. Scope of this Section. This Section addresses provisions governing retaliation and pretaliation against whistleblowers. This Section does do not cover whistleblower-award provisions. Government authorities' ability to offer bounties to whistleblowers is governed by statute. Statutes authorizing bounties are relatively rare. Moreover, the existing statutes that permit whistleblower awards differ materially from each other, including on fundamental questions such as whether the whistleblower can bring a private action on behalf of the government and whether the whistleblower's identity should remain anonymous. Thus, this Section does not make recommendations to government authorities about to how to implement whistleblower-award programs because officials with authority to do so tend to be operating within the constraints of statutes that different materially from each other.

b. Defining "whistleblower" and "retaliation". A whistleblower is a person who provides any information to:

(a) relevant government authorities about any activity or conduct that that person reasonably and in good faith believes to be a violation of any laws applicable to the organization; or

(b) the organization about any activity or conduct that that person reasonably and in good faith reasonably believes to violate:

(1) laws applicable to the organization; or

(2) the organization's own ethical rules or internal standards of conduct.

Whistleblower protections also should apply to people who in good faith provide information to any government authority investigating an organization's misconduct or to internal investigators engaged in an ongoing inquiry that is relevant to the government investigation, whether or not the person believes the organization engaged in misconduct. Employees and agents should be protected against retaliation if they provide information about misconduct that they reasonably and in good faith believe is or may be occurring, even if they are mistaken.

Retaliatory action/retaliation includes but is not limited to any adverse action taken by the organization against a whistleblower if the organization's knowledge that the individual was, or

was likely to be, a whistleblower was a contributing factor in its decision to pursue an adverse action. Prohibited retaliation also includes actions that have the effect of discouraging employees from reporting misconduct, as discussed in Comment *f*.

These definitions are consistent with The Principles of the Law, Government Ethics § 715.

c. Anonymity of whistleblowers. There are many reasons why whistleblowers who come forward to reveal confidential information about an organization to a government authority may desire that their identities not be revealed to the public or their employers even if they are legally protected against retaliation. They may still work at the organization and wish to avoid imperiling their jobs or suffering more subtle negative consequences. They may have friendships with people still in the organization that would be damaged if their identities were revealed. They may fear that being revealed as "snitches" may harm their prospects of being employed elsewhere. Wherever possible, government officials should protect the identity of a whistleblower for as long as possible. Ideally, the whistleblower's identity should never be disclosed to the organization or should not be disclosed until a whistleblower award is paid to the whistleblower.

In situations in which enforcement officials cannot investigate or bring an enforcement actions without providing information to the organization that could reveal the whistleblower's identity, they should affirmatively remind the employer, and the high-level and substantial authority personnel with whom they deal, about the legal prohibitions against retaliating against suspected whistleblowers and the potential consequences for organizations and individuals who violate them.

d. Importance of protecting against retaliation. Government authorities encourage whistleblowing by giving assurances that persons who provide sensitive information to them will not thereafter suffer retaliation. Accordingly, government authorities should establish and publicize whistleblower-protection policies. Protections against retaliation include civil rights of action, government enforcement actions, and safeguards against adverse employment actions. Government authorities may require a regulated organization to disclose whistleblower-protection policies to its employees and agents.

e. Prohibited forms of retaliation. Whistleblower protections apply to actions directed against the whistleblower that are at least in part a response to the whistleblowing. For example, if an employer terminates a whistleblower without knowing or suspecting that the person had

provided or information to a government authority, the whistleblower cannot claim the protection of a nonretaliation rule. By contrast, a retaliatory motive need not be the sole reason for the negative action taken against the whistleblower. It should be sufficient to trigger these protections if the party that is inflicting harm on the whistleblower is motivated in part by hostility stemming from the whistleblowing, even if other motivations also were present.

Illustration:

1. An employee of a university, A, informs the accreditation agency that the university has understated it student−teacher ratios. A's job is already in jeopardy because she finds it difficult to work with others in a team setting. When A's superior learns of A's report to the accreditation agency, the supervisor declares this to be the "last straw" and terminates A from her job. A can claim whistleblower protection against retaliation because even though the employer had other, potentially benign, reasons for terminating her, part of the motivation behind the job action was anger at A for whistleblowing.

f. Nondisclosure/nondisparagement agreements. Organizations often have valid reasons for requiring employees not to disclose confidential information obtained during the course of employment, and for prohibiting employees or former employees from disparaging the organization. But organizations must ensure that all confidentiality and non-disparagement clauses in agreements with employees expressly state that the clause does not apply to any action taken by the employee to bring suspected misconduct to the attention of either government authorities or a self-regulatory organization with jurisdiction over the organization. Contracts with employees that threaten them with costs should they disclose confidential information in the course of reporting misconduct to government authorities constitute a form of preemptive retaliation for whistleblowing, referred to as pretaliation.

Several factors counsel strongly in favor of explicit provisions in nondisclosure or nondisparagement agreements stating that they do not prohibit employees from reporting misconduct to government authorities or self-regulatory bodies. Such provisions reinforce a culture of compliance within the organization and help deter misconduct. Failing to exclude communications with government authorities or self-regulatory bodies may be viewed as a signal that the organization wishes to discourage whistleblowing.

However, any exclusion for communications with government authorities or self-regulatory bodies should not be construed as a waiver of the organization's attorney–client privilege. It is appropriate for attorneys representing an organization in a government investigation to instruct employee witnesses to maintain the confidentiality of attorney–client communications in order to avoid any claim of waiver. In some cases, pretaliation agreements may be prohibited by law. For example, Securities and Exchange Commission Rule 21F-17—implementing a provision of the Dodd–Frank Wall Street Reform and Consumer Protection Act—states that "[n]o person may take any action to impede an individual from communicating directly with the Commission staff about a possible securities law violation, including enforcing or threatening to enforce a confidentiality agreement … with respect to such communications."

For a discussion of best practices for organizations' internal-reporting systems and policies against retaliation, see § 5.18.

g. Protections for internal as well as external reporting. To the extent allowed by law, civil and administrative authorities should protect employees and other agents from retaliation whether they report externally to government authorities or internally to the organization.

To the extent allowed by law, civil and administrative authorities can seek to encourage reporting to the government by offering whistleblower awards to employees if they either provided information about potential misconduct directly to the government or reported the information to the organization, which in turn reported to government authorities, provided that the internal report was a substantial factor in informing the government about material misconduct and resulted in a successful enforcement resolution.

h. Protections for information that would not qualify for an award. Whistleblower protections against retaliation should apply when a purported whistleblower has provided potentially valuable, credible information to the government. It is not necessary that this information qualify for a whistleblower award, if the government authority has power to make such awards. At the time he or she comes forward, the whistleblower may not know whether the information he or she is providing is already in the hands of the government, whether it will be useful in a subsequent enforcement proceeding, or whether the government's enforcement efforts will be successful. Protections against retaliation would be undermined if whistleblowers could rely on them only if the information leads to a successful enforcement action. The information

provided by the whistleblower must, however, be credible, be made in good faith, and be of potential value in exposing a violation of law.

i. Organization's ability to investigate internally reported misconduct. Organizations can help protect employees who report suspected misconduct from retaliation by creating internal-reporting systems that allow for anonymous reporting, as discussed in § 5.18. Nevertheless, circumstances can arise in which the organization cannot effectively investigate the reported suspected misconduct without creating a risk that other employees will suspect that the whistleblowing employee reported the misconduct. This risk is particularly great when the employee made objections about the misconduct to others in the organization outside of the internal-reporting system. An organization that proceeds to investigate material misconduct in this situation should not be deemed to be acting in a retaliatory fashion against the whistleblowing employee if it takes all reasonable measures to protect the person's identity, consistent with its legal obligation to investigate and terminate violations of the law. The organization should proactively take steps to protect the employee from explicit or implicit retaliation, including ostracism, in such circumstances. Sometimes, the organization may be most able to effectively protect the employee and emphasize its commitment to compliance by giving the employee a desirable (and desired) promotion. In other situations, the organization can proactively protect the employee from direct or indirect retaliation in the short run and provide longer-run protections by taking appropriate disciplinary measures against all employees who committed, conspired to commit, or knowingly condoned the misconduct or had knowledge of misconduct committed by employees under their supervision and knowingly failed to act to terminate it.

j. Protections for employees who report on activities of other organizations. In general, nonretaliation policies cover actions by organizations that employ the whistleblower or by employees and agents of those organizations. The scope of whistleblower protections can extend further, however. They may, for example, cover employees of companies in a contractual relationship with the organization. A nonretaliation policy could even extend to other individuals, regardless of their relationship with the organization, on the theory that there is no social value in retaliation against whistleblowers. As the scope of coverage increases, however, it will become increasingly difficult for a whistleblower to establish that the harm experienced was due to retaliation for whistleblowing rather than some other reason.

Illustration:

2. Whistleblower A is an employee of a biomedical laboratory that provides testing services for hospital research studies. A tells a government authority that one of the hospital's research projects has failed to comply with a mandatory experimental protocol. The government authority commences an investigation into the charges. A's employer has reason to suspect that A is the source of the information. A few months later, A is terminated on grounds of persistent tardiness and falsification of expense-account records. A may claim protection of the government authority's whistleblower policy if the policy covers employees of contractors with entities under the authority's jurisdiction. To prevail on her claim, however, A must persuade the trier of fact that the adverse employment decision was at least partially a result of A's whistleblowing rather than entirely for some legitimate reason.

REPORTERS' NOTES

a. Internal policies on nonretaliation. For a discussion of best practices for organization's internal-reporting systems and policies against retaliation see § 5.18.

b. Retaliation as a significant concern. Notwithstanding legal prohibitions on retaliation, actual retaliation and the perceived threat of retaliation remain significant impediments to efforts to encourage employees to report organizational misconduct. See Rachel Louise Ensign, *Survey: Companies Finding More Whistleblower Retaliation*, WALL STREET J. RISK & COMPLIANCE BLOG (Mar. 9, 2015, 6:21 PM), https://www.wsj.com/articles/BL-252B-6407; see also ETHICS RES. CTR., NATIONAL BUSINESS ETHICS SURVEY, 13, 34 (2014) http://www.ethics.org/research/eci-research/nbes/nbes-reports/nbes-2013 (indicating fear amongst and relatively high levels of retaliation against those who report misconduct through internal channels).

c. Restatement of the Law, Employment Law. The Restatement of the Law, Employment Law addresses protections for whistleblowers under the sections providing for liability in tort for wrongful discharge in violation of public policy. Restatement of the Law, Employment Law §§ 5.01–5.03 (AM. L. INST. 2015).

Section 5.02 sets forth a list of protected activities that employers cannot discharge an employee for undertaking without being subject to liability for wrongful discharge. The protected activities include "report[ing] or inquir[ing] about conduct that the employee reasonably and in good faith believes violates a law or an established principle of a professional or occupational code of conduct protective of the public interest." Restatement of the Law, Employment Law § 5.02 (AM. L. INST. 2015).

Section 5.02, Comment *f* states that in order to be protected, the employee must act reasonably in reporting the illegal conduct. The factors relevant to whether the employee's conduct is protected include:

> (1) whether the employee reported the matter in good faith believing that the employer's conduct was illegal;
> (2) whether the employee's belief was reasonable; and
> (3) whether the employee made the report in a reasonable manner.

Restatement of the Law, Employment Law § 5.02, Comment *f* (AM. L. INST. 2015).

Section 5.02, Comment *f* further states that "[i]f the belief and manner of reporting are reasonable, and the employee acted in good faith, then the employee's report is protected under this subsection." Id.

Under Section 5.02, an employee is not protected if the employee believes the reported conduct is merely unwise or inappropriate rather than illegal, or if the employee believes the conduct is illegal but the belief is either unreasonable or not held in good faith. Id. An employee who blows the whistle based on a reasonable and good-faith belief that his or her employer is engaging in illegal conduct is protected, however, even if that belief is mistaken. Comment *g* explains that:

> Requiring employees to be correct in assessing illegality would unduly chill them from acting in the public interest. Employees usually are not trained in the law and lack access to all the relevant facts. Extending protection to employees with mistaken but reasonable, good-faith beliefs about the employer's illegal conduct encourages such reports and thereby curbs the incidence of illegal acts.

Restatement of the Law, Employment Law § 5.02, Comment *g* (AM. L. INST. 2015).

Section 5.01, Comment *b* provides that an employer's decision to discharge an employee who reported misconduct is only actionable if: (a) the employer knows of the employee's participation, or plan to participate, in the protected activity, and (b) discharges the employee because of that participation or plan to participate. The employer's intent to punish or deter protected activity is an element of the claim. Restatement of the Law, Employment Law § 5.01, Comment *b* (AM. L. INST. 2015).

d. Government employees: The Principles of the Law, Government Ethics § 713 and § 715, Comment *a*, also recognize the importance of enabling whistleblowers to provide information confidentially and of protecting them from a broad range of retaliatory acts. Principles of the Law, Government Ethics § 713, § 715, Comment *a* (AM. L. INST., Tentative Draft No. 3, 2021).

e. Coverage. On whistleblower protections for employees of contractors or subcontractors with an organization, see Lawson v. FMR LLC, 571 U.S. 429 (2014) (whistleblower protections of Sarbanes-Oxley Act of 2002 apply to employees of contractors and subcontractors to public companies).

f. Whistleblower protections: anonymity and confidentiality. The whistleblower-award regime of the Dodd–Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) also includes protections for whistleblowers. Whistleblowers are allowed to submit their information anonymously and remain eligible for an award if they are represented by counsel. See 15 U.S.C. § 78u-6(d)(2); 17 C.F.R. §§ 240.21F-7(b), 240.21.F-9(c). In addition, the Securities and Exchange Commission (SEC) is committed to keeping whistleblowers' identity confidential to the fullest extent possible. The SEC will not disclose a whistleblower's identity in response to a Freedom of Information Act request. Nevertheless, the SEC's use of the information provided during its investigation may indirectly reveal the person's identity. The whistleblower's identity may come to light through documents produced during legal proceedings. https://www.sec.gov /whistleblower/frequently-asked-questions#faq-7.

g. Dodd-Frank antiretaliation provisions. The earliest whistleblower programs recognized the need to protect whistleblowers from retaliation. For example, the qui tam provisions of the False Claims Act contain language prohibiting retaliation against whistleblowers. 31 U.S.C. § 3730(h).

The Dodd-Frank Act includes antiretaliation provisions that protect people in the United States who report to government authorities. 15 U.S.C. § 78u-6(h)(1)(C). An individual who reports internally to his or her firm, and then later reports to the SEC, can qualify as a whistleblower if he or she reports to the SEC within 120 days of reporting to the firm. But in Digital Realty Trust, Inc. v. Somers, 583 U.S. (2018), the U.S. Supreme Court ruled that Dodd-Frank's antiretaliation provisions only apply to employees who report to the SEC, and not to those who have only reported internally. As a result, an employee who is terminated after making an internal report but before he or she reports to the SEC would not have a valid antiretaliation claim under Dodd-Frank, but might be entitled to a whistleblower award.

Employees who report internally are not necessarily without recourse, however. They may be protected by the Sarbanes-Oxley Act of 2002, which prohibits certain companies from retaliating against an employee who "provid[es] information … or otherwise assist[s] in an investigation regarding any conduct which the employee reasonably believes constitutes a violation" of certain delineated fraud statutes, any SEC rule or regulation, or "any provision of Federal law relating to fraud against shareholders." The protections of Sarbanes-Oxley are weaker than those of Dodd-Frank, however, as the former includes an administrative-exhaustion requirement and limits recovery to back pay with interest, as opposed to two-times back pay with interest. 18 U.S.C. § 1514A - Civil action to protect against retaliation in fraud cases.

h. SEC position on employment contracts that discourage reporting. SEC Rule 21F-17 prohibits covered persons from taking any actions to prohibit or impede someone from reporting to the agency. Firms violate the law if they require employees to sign a contract that prevents disclosure of the firm's private information to outsiders unless it makes clear that employees are not prohibited from reporting misconduct to authorities such as the SEC. A firm can also violate the law if its internal-reporting system or internal investigation requires employees to keep matters confidential (including from the SEC).

The SEC has filed a variety of enforcement actions against companies found to have contract language that stifles whistleblowing communications. For example, in the 2015 action *In re KBR*, the SEC sanctioned KBR Inc. for including the following confidentiality clause in its internal-reporting system:

> I understand that in order to protect the integrity of this review, I am prohibited from discussing any particulars regarding this interview and the subject matter discussed during the interview, without the prior authorization of the Law Department. I understand that the unauthorized disclosure of information may be grounds for disciplinary action up to and including termination of employment.

The SEC sanctioned the company because the clause had a chilling effect without first establishing that any employee had been sanctioned for violating the clause. The SEC required the company to ensure that its confidentiality clause affirmatively informed employees of their right to report:

> Nothing in this Confidentiality Statement prohibits me from reporting possible violations of federal law or regulation to any governmental agency or entity, including but not limited to the Department of Justice, the SEC, the Congress, and any agency Inspector General, or making other disclosures that are protected under the whistleblower provisions of federal law or regulation. I do not need the prior authorization of the Law Department to make any such reports or disclosures and I am not required to notify the company that I have made such reports or disclosures.

In re KBR, Inc., Exchange Act Release No. 74619, 2015 WL 1456619 (Apr. 1, 2015), https://www.sec.gov/litigation/admin/2015/34-74619.pdf.

In 2017, the SEC sanctioned BlackRock Inc. based on a clause in a separation agreement that stated that the employee waived any right to recovery of incentives for reporting of misconduct, including, without limitation, under the Dodd-Frank Act and the Sarbanes-Oxley Act of 2002, relating to conduct occurring prior to the date of the agreement. https://www.sec.gov/news/pressrelease/2017-14.html.

In the same year, the SEC sanctioned HomeStreet Inc. for entering into an indemnification agreement with an employee that stated that the firm would pay for an employee's counsel if, but only if, the employee confirmed that he was not a whistleblower. Sec. & Exchange Comm'n, Financial Company Charged with Improper Accounting and Impeding Whistleblowers, SEC 17-24, 2017 WL 218598 (Jan. 19, 2017), https://www.sec.gov/news/pressrelease/2017-24.html. The firm's post-settlement provisions on indemnification provide:

- Employee understands that nothing contained in this Agreement limits Employee's ability to file a charge or complaint with any federal, state or local governmental agency or commission ("Government Agencies");
- Employee further understands that this Agreement does not limit Employee's ability to communicate with any Government Agencies or otherwise participate in any investigation or proceeding that may be commenced by any Government

> Agency including providing documents or other information without notice to the Company; and
> - This Agreement does not limit the Employee's right to receive an award for information provided to any Government Agencies.

i. Whistleblower protections under state laws. Many states have statutes that prohibit making false claims to the government that include protections for those who report fraud to the government. For example, the California False Claims Act states that whistleblowers are entitled to job protection if any "employee, contractor, or agent is discharged, demoted, suspended, threatened, harassed, or in any other manner discriminated against in the terms and conditions of his or her employment." CAL. GOV'T CODE § 12653. Under California law, whistleblowers who are retaliated against are entitled to reinstatement with the same seniority status, two times the amount of back pay, as well as interest on the back pay, compensation for any special damages, and, when appropriate, punitive damages. The company that violated the law also must pay the whistleblower's litigation costs and attorneys' fees.

Under New Jersey's Conscientious Employee Protection Act, an employee is protected from acts of retaliation—such as being fired, demoted, passed up for protection, or harassed—if he or she:

> (a) discloses or threatens to disclose to a supervisor or public body conduct or a policy that the employee reasonably believes violates the law;
> (b) provides information to any public body investigating or conducting a hearing or inquiry into a legal violation;
> (c) provides information involving deception or misrepresentation to any shareholder, investor, client, patient, customer, employee, former employee, retiree or pensioner of the employer or any governmental entity;
> (d) provides information regarding any perceived criminal or fraudulent activity, policy or practice of deception or misrepresentation which the employee reasonably believes may defraud any shareholder, investor, client, patient, customer, employee, former employee, retiree or pensioner of the employer or any governmental entity; or
> (e) Objects to, or refuses to participate in, any activity, policy or practice which the employee reasonably believes:
>
> > (1) is in violation of a law, or a rule or regulation issued under the law or, if the employee is a licensed or certified health care professional, constitutes improper quality of patient care;
> > (2) is fraudulent or criminal; or
> > (3) is incompatible with a clear mandate of public policy concerning the public health, safety or welfare or protection of the environment.

N.J. STAT. ANN. § 34:19-3.

The protection against retaliation, when a disclosure is made to a public body, does not apply unless the employee has brought the activity, policy, or practice to the attention of his or her

supervisor by written notice and given the employer a reasonable opportunity to correct the activity, policy, or practice. However, disclosure is not required when the employee reasonably believes that the activity, policy, or practice is known to one or more employees of the organization with supervisory authority or when the employee fears physical harm as a result of the disclosure, provided that the situation is emergency in nature.

State-law protections against retaliation vary in their effectiveness, however, depending in part on the rules for determining whether a negative action against a whistleblower can be deemed retaliatory. Some states deem an official action retaliatory if the whistleblowing was a contributing cause of the negative action against the employee. Yet others require that it be the "sole cause"—a standard that undermines protections for whistleblowers and thereby undermines incentives to report misconduct. See Nancy M. Modesitt, *Causation in Whistleblowing Claims*, 50 U. RICH. L. REV. 1193, 1201-1210, 1225 (2016); see also Principles of the Law, Government Ethics § 715, Reporters' Note *a* (AM. L. INST., Tentative Draft No. 3, 2021).

j. Other whistleblower programs. Many other government programs or regulatory statutes provide whistleblowers with assurances against retaliation. See Occupational Safety and Health Administration, The Whistleblower Protection Programs, available at http://www.whistleblowers.gov/wb_filing_time_limits.html. Federal whistleblower protections include:

- Occupational Safety & Health Act, 29 U.S.C. § 660(c);
- Asbestos Hazard Emergency Response Act, 15 U.S.C. § 2651;
- Clean Air Act, 42 U.S.C. § 7622;
- Comprehensive Environmental Response, Compensation and Liability Act, 42 U.S.C. § 9610;
- Energy Reorganization Act, 42 U.S.C. § 5851;
- Federal Water Pollution Control Act, 33 U.S.C. § 1367;
- Safe Drinking Water Act, 42 U.S.C. § 300j-9(i);
- Solid Waste Disposal Act, 42 U.S.C. § 6971;
- Toxic Substances Control Act, 15 U.S.C. § 2622;
- Federal Railroad Safety Act, 49 U.S.C § 20109;
- International Safe Container Act, 46 U.S.C. § 80507;
- Moving Ahead for Progress in the 21st Century Act, 49 U.S.C. § 30171;
- Pipeline Safety Improvement Act, 49 U.S.C. § 60129;
- Seaman's Protection Act, 46 U.S.C. § 2114;
- Surface Transportation Assistance Act, 49 U.S.C § 31105;
- Wendell H. Ford Aviation Investment and Reform Act for the 21st Century, 49 U.S.C. § 42121;
- Affordable Care Act, 29 U.S.C. § 218C;
- Consumer Financial Protection Act, 12 U.S.C. § 5567;
- Sarbanes-Oxley Act, 18 U.S.C. § 1514A;
- Consumer Product Safety Improvement Act, 15 U.S.C. § 2087;

• FDA Food Safety Modernization Act, 21 U.S.C. § 399d.

k. International comparison. In the United Kingdom, retaliation against a whistleblower is prohibited. In addition, the Enterprise Regulatory Reform Act of 2013 imposes vicarious liability on employers for any negative actions taken by coworkers against a worker who made a protected disclosure. The company will have a defense if it took all reasonable steps to prevent the detrimental treatment. In addition, companies are now prohibited from including any clause in a nondisclosure agreement with an employee that is designed to prevent the employee from making a whistleblower disclosure. Companies under the jurisdiction of the Financial Conduct Authority have to ensure that any settlement agreement with an employee clarifies that nothing in that agreement prevents the worker from making a protected whistleblowing disclosure. Jillian Naylor, et. al, *Whistleblower: The U.K. Perspective*, THE PRACTITIONER'S GUIDE TO GLOBAL INVESTIGATIONS (4th ed. 2020).