

# Paying the Price: Should Corporations' Payment of Their Employees' Legal Fees be a Factor in Corporate Indictment Decisions?

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## INTRODUCTION

Business organizations<sup>1</sup> in the United States may be held criminally liable for the misconduct of their employees.<sup>2</sup> In the past decade, the executive branch has seen fit to devise a set of guidelines to provide federal prosecutors with a systematic method for determining whether to, in fact, bring criminal charges against a corporation for the criminal deeds of its employees.<sup>3</sup> In recent years much controversy has erupted over a number of these guidelines. Most of the institutional advocacy and legal scholarship to date has focused on the implications of federal prosecutors in making their indictment decision, taking into consideration whether a corporation has agreed to waive its attorney-client privilege.<sup>4</sup> In 2006, however, the judiciary and Congress joined the fracas by calling into question the legitimacy of another guideline, one that draws prosecutors'

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1. Throughout this Note, I will often use terms such as corporation, firm, and entity interchangeably. I do so in accordance with the statutory definition of organizations subject to criminal liability, under which all such bodies qualify. *See* 18 U.S.C. § 18 (2000).

2. *See infra* notes 116–17 and accompanying text. *See also* 1 KATHLEEN F. BRICKEY, CORPORATE CRIMINAL LIABILITY 89–118 (1991) [hereinafter BRICKEY, CORPORATE LIABILITY] (providing a general overview of the imputation of criminal conduct to corporations).

3. *See infra* notes 9, 28, 104 and accompanying text.

4. *See infra* notes 15, 47.

attention to whether employers have advanced the legal fees of their employees<sup>5</sup> under investigation.<sup>6</sup>

While it would be ideal to simply provide that any prosecutorial consideration that could marginally infringe on a corporation or its employees' rights should not be a factor in indictment decisions, the answer is not that simple. One need look no further than Enron and the ensuing wave of similarly devastating financial crimes committed by corporations in recent years to see that the need for effective enforcement is paramount.<sup>7</sup> Accordingly, it is more crucial now than ever to find a proper balance between protecting individual rights and recognizing legitimate law enforcement endeavors. This Note sets out to do just that by focusing on the emerging issue of employee legal fee advancement as an appropriate prosecutorial consideration.

Part I of this Note surveys the development of federal prosecutorial guidelines for corporations. It begins by discussing the first set of formal guidelines for corporate indictment decisions, promulgated in 1999, and the policies that were incorporated therein. Next, this section considers the events that began to unfold shortly thereafter, namely the massive influx of corporate scandals beginning with Enron's collapse in 2001 and how the executive branch responded. Part I concludes with an overview of what, until recently, were the revised corporate prosecutorial guidelines, developed in 2003, to combat the evolution in corporate financial crime.

Part II outlines the reaction these revised guidelines received from the private sector and eventually the judiciary and Congress. This section describes the major criticisms and arguments that have been levied against using the advancement of legal fees as a factor in corporate indictment decisions, as well as several alternatives that have been proposed. Part II closes with the executive branch's recent response to these criticisms—the promulgation of the current guidelines.

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5. For ease of expression, the term "employee(s)" in this Note refers to a current or former agency relationship between the individual and the business entity. In addition to lower level employees, an agency relationship exists between employers and directors, officers, and partners. *See* RESTATEMENT (THIRD) OF AGENCY § 1.01(c) (2006).

6. *See infra* Part II.B–C.

7. *See infra* Part I.B.

Part III analyzes the arguments that have been raised against the consideration of legal fee advancement. It starts by fleshing out the arguments' underlying premises to examine their validity, and then turns to the alternatives that have been proposed, evaluating each to determine if it would serve as an effective solution. Part IV begins by suggesting a new standard, and then proceeds to compare that standard both with the goals that have been outlined throughout this Note, as well as the other solutions that have been offered. The proposal introduced by this Note, I conclude, best reaches a balance between protecting the interests of corporations and their employees, while at the same time allowing prosecutors to consider legal fee advancement in the appropriate context.

#### I. THE DEVELOPMENT OF FEDERAL PROSECUTORIAL GUIDELINES FOR CORPORATE ENTITIES

##### A. *Guidelines Pre-Enron*

Prior to 1999, the United States Department of Justice ("DOJ") did not have a formal policy in place to evaluate criminal conduct by corporate entities for the purpose of making prosecutorial decisions.<sup>8</sup> In 1999, the DOJ set out to provide this missing guidance in a memorandum authored by then Deputy Attorney General Eric Holder ("Holder Memo").<sup>9</sup> The Holder Memo laid out "factors [that] should generally inform a prosecutor in making the decision whether to charge a corporation in a particular case."<sup>10</sup> While not outcome-

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8. See *infra* text accompanying notes 17–24 for a discussion of federal prosecutorial policy with regard to corporate entities prior to 1999.

9. Memorandum from Eric Holder, Deputy Att’y Gen., to all U.S.D.O.J. Component Heads and U.S. Att’ys (June 16, 1999) [hereinafter Holder Memo] (on file with the U.S.D.O.J.), available at <http://www.usdoj.gov/criminal/fraud/fcpa/append/ix/appendixK.pdf>. The Holder Memo identifies the “great benefits” that come from “vigorous enforcement” of criminal laws against corporations. *Id.* § I.A. The guidelines promulgated in the Holder Memo were likely an effort to create “a more systematic approach to handling criminal violations by corporations.” Mary Robeck et al., *Corporate Cooperation in the Face of Government Investigations*, 17 HEALTH LAW. 20, 21–22 (2005). See *infra* notes 17–24 and accompanying text for a discussion of the decidedly unsystematic approach that federal prosecutors employed in corporate criminal indictment decision-making before the Holder Memo was promulgated.

10. Holder Memo, *supra* note 9, at introductory cmt.

determinative or binding on prosecutors,<sup>11</sup> these factors were designed to “provide a useful framework” in which prosecutors could analyze cases.<sup>12</sup>

The Holder Memo identifies eight factors that may be relevant to prosecutors when determining whether to bring charges.<sup>13</sup> Of significance is the fourth factor, which draws prosecutorial attention to “[t]he corporation’s timely and voluntary disclosure of wrongdoing and its willingness to cooperate with the government’s investigation of its agents . . . .”<sup>14</sup> The Holder Memo provides guidance on how to assess a corporation’s cooperation, namely “whether the corporation appears to be protecting its culpable employees and agents.”<sup>15</sup> It states:

Thus, while cases will differ depending on the circumstances, a corporation’s promise of support to culpable employees and agents, either through the advancing of attorneys fees, [or]

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11. *Id.* See also Nancy Kestenbaum & Jason P. Criss, *Credit Where Credit is Due? The Role of Internal Investigations in the Outcome of Government Investigations*, 1564 CORP. L. & PRAC. COURSE HANDBOOK SERIES, 152 n.2 (2006) (“[T]he Holder Memo provided guidance . . . but was not binding.”).

12. See Holder Memo, *supra* note 9, at introductory cmt.

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[P]rosecutors should consider the following factors in reaching a decision as to the proper treatment of a corporate target: 1. The nature and seriousness of the offense, . . . 2. The pervasiveness of wrongdoing within the corporation, . . . 3. The corporation’s history of similar conduct, . . . 4. The corporation’s timely and voluntary disclosure of wrongdoing and its willingness to cooperate in the investigation of its agents, . . . 5. The existence and adequacy of the corporation’s compliance program, . . . 6. The corporation’s remedial actions, . . . 7. Collateral consequences, . . . and 8. The adequacy of non-criminal remedies . . . .

*Id.* § II.A.

14. *Id.* § II.A.4. As justification for the relevancy of this factor, the Holder Memo states:

In investigating wrongdoing by or within a corporation, a prosecutor is likely to encounter several obstacles resulting from the nature of the corporation, itself. It will often be difficult to determine which individuals took which action on behalf of the corporation. . . . Accordingly, a corporation’s cooperation may be critical in identifying the culprits and locating relevant evidence.

*Id.* § VI.B. The Holder Memo makes clear, however, that “a corporation’s willingness to cooperate is merely one relevant factor, one that needs to be considered in conjunction with other factors.” *Id.*

15. *Id.* Another factor that the Holder Memo identifies in assessing the adequacy of a corporation’s cooperation is “the completeness of its disclosure including, if necessary, a waiver of the attorney-client and work product protections . . . .” *Id.*

through retaining the employees without sanction for their misconduct. . . may be considered by the prosecutor in weighing the extent and value of a corporation's cooperation.<sup>16</sup>

While novel in its approach to provide an explicit framework of analysis for the treatment of target corporations, the Holder Memo was modeled after well-established prosecutorial principles. Indeed, prior to the inception of the Holder Memo, the analysis for corporate prosecutorial decisions was treated in much the same way as individual prosecutions—guided by DOJ policy found in the United States Attorney's Manual ("USAM").<sup>17</sup> The USAM section titled "Principles of Federal Prosecution" states that prosecutors should consider an individual's willingness to cooperate when making the decision whether to initiate or decline prosecution.<sup>18</sup>

Moreover, in 1991, seven years before the inception of the Holder Memo, the United States Sentencing Commission<sup>19</sup> amended the Federal Sentencing Guidelines, adding a new chapter titled "Sentencing of Organizations" ("Organizational Guidelines").<sup>20</sup> The Organizational Guidelines filled a void in the Federal Sentencing Guidelines by serving as a guide for federal courts sentencing

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16. *Id.* (footnote omitted). Importantly, the Holder Memo distinguishes between corporations that voluntarily pay the legal fees of their officers and those that are required under state law to pay the fees. *Id.* § VI.B n.3. For corporations that are mandated by state law to pay the legal fees of their officers, such payment should not be considered by prosecutors as indicative of non-cooperation. *Id.*

17. See U.S. DEP'T OF JUSTICE, U.S. ATT'YS' MANUAL § 9-27.00 (2005) [hereinafter U.S. ATT'YS' MANUAL]; see also Lawrence D. Finder, *Internal Investigations: Consequences of the Federal Deputation of Corporate America*, 45 S. TEX. L. REV. 111, 113–14 (2003) (describing DOJ practices outlined in the USAM). The Holder Memo explicitly incorporates the considerations outlined in the USAM, stating, "Generally prosecutors should apply the same factors in determining whether to charge a corporation as they do with respect to individuals." Holder Memo, *supra* note 9, § II.A.

18. U.S. ATT'YS' MANUAL § 9-27.230B6 ("A person's willingness to cooperate in the investigation or prosecution of others is another appropriate consideration in the determination whether a Federal prosecution should be undertaken."); cf. *id.* § 9.27.420B1 ("The defendant's willingness to provide timely and useful cooperation as part of his/her plea agreement should be given serious consideration.").

19. The United States Sentencing Commission is an independent agency in the judicial branch charged with developing guidelines and policy statements for courts to use when "sentencing offenders convicted of federal crimes." U.S. SENTENCING GUIDELINES MANUAL § 1A1.1 cmt. background (2005).

20. SENTENCING GUIDELINES MANUAL § 8 (amended 1991) [hereinafter Organizational Guidelines].

corporate entities.<sup>21</sup> Among other things, the Organizational Guidelines strongly promote and incentivize cooperation and acceptance of responsibility by corporate defendants.<sup>22</sup> Importantly, the Organizational Guidelines also call for an effective compliance program,<sup>23</sup> which includes “appropriate incentives” for employees to perform in accordance with the program and “appropriate disciplinary measures” for employees engaging in criminal conduct.<sup>24</sup> Thus, the consideration in the Holder Memorandum of a corporation’s cooperation and measures to determine the authenticity of that cooperation was a logical extension of the considerations that were already embedded within the criminal justice system.

### *B. Enron Changes the Landscape*

The issue of criminal conduct of corporations and their employees took center stage in December 2001, when Enron, then the nation’s seventh largest corporation, filed for bankruptcy.<sup>25</sup> The bankruptcy came amidst rumors of a widespread accounting scandal after the company announced a \$618 million net loss for the third quarter of 2001.<sup>26</sup> When the dust settled, the company’s collapse cost its shareholders \$68 billion and thousands of employees lost their jobs

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21. *Id.* app. C, amend. 422 (“This [A]mendment adds guidelines and policy statements to address the sentencing of organizational defendants.”). The Supreme Court has since held that the Organizational Guidelines are merely advisory. *See* *United States v. Booker*, 543 U.S. 220, 259 (2005).

22. *See, e.g.*, Organizational Guidelines, *supra* note 20, § 8C2.5(g) (granting a reduction in the organization’s “culpability score” for reporting offenses to government authorities, fully cooperating in the investigation, and “clearly demonstrated recognition and affirmative acceptance of responsibility”). As one commentator opined, prior to the Holder Memo, “[t]he Organizational Guidelines, with their attention to corporate cooperation, also operated as a type of paradigm for federal prosecutors who saw in them some direction in making corporate charging decisions caused by the void in DOJ policy.” Finder, *supra* note 17, at 114.

23. An effective compliance program, under the Organization Guidelines, requires an organization to “exercise due diligence to prevent and detect criminal conduct” and “otherwise promote an organizational culture that encourages . . . compliance with the law.” Organizational Guidelines, *supra* note 20, § 8B2.1(a).

24. *Id.* § 8B2.1(b)(6).

25. Voluntary Petition, *In re Enron Corp.*, No. 01-16034 (AJG) (Bankr. S.D.N.Y. filed Dec. 2, 2001).

26. Kathleen F. Brickey, *From Enron to WorldCom and Beyond: Life and Crime after Sarbanes-Oxley*, 81 WASH. U. L.Q. 357, 360–62 (2003) [hereinafter Brickey, *From Enron to WorldCom*].

and retirement funds.<sup>27</sup> This loss, staggering in its own right, seems magnified by the fact that it was caused by the criminal conduct of corporate fiduciaries.<sup>28</sup>

As soon became clear, Enron was not an anomaly, but rather the first major indication of a seemingly pervasive pattern of criminal activity across corporate America.<sup>29</sup> Less than a year after Enron's bankruptcy, WorldCom, another Fortune 500 company and telecommunications powerhouse, filed for bankruptcy after announcing a \$3.8 billion accounting restatement.<sup>30</sup> Like Enron, the company's downfall was brought about by the criminal behavior of its executives, cost hundreds of thousands of investors billions of dollars, and eliminated thousands of jobs and employee retirement

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27. Thomas S. Mulligan, *The Enron Verdicts; Enron's Top Executives are Convicted of Fraud*, L.A. TIMES, May 26, 2006, at A1. For an in-depth discussion of the Enron scandal and its financial impact, see John Kroger, *Enron, Fraud, and Securities Reform: An Enron Prosecutor's Perspective*, 76 U. COLO. L. REV. 57 (2005); BETHANY MCLEAN & PETER ELKIND, *SMARTEST GUYS IN THE ROOM: THE AMAZING RISE AND SCANDALOUS FALL OF ENRON* (2003).

28. See generally *Regal-Beloit Corp. v. Drecoli*, 955 F. Supp. 849, 857–58 (N.D. Ill. 1996) (“It is a well-established common law principle that corporate officers and directors owe a fiduciary duty of utmost good faith and loyalty to their corporations.” This “implies that the [corporation] has reposed some trust or confidence in the agent.”). In Enron's case sixteen former officers and directors, including Chief Financial Officer Andrew Fastow, Chief Accounting Officer Richard Causey, Chief Executive Officer Jeffrey Skilling, and Chairman Kenneth Lay, were convicted of federal criminal offenses stemming from their activities at Enron. Mulligan, *supra* note 27.

29. See generally Brickey, *From Enron to WorldCom*, *supra* note 26, at 358 (“In the beginning, it was widely assumed that the Enron scandal was an anomaly. But it soon became clear that this was anything but an isolated case of financial accounting fraud at a major corporation.”); Nancy Browning, *Developments in Corporate Scandals in 2004*, 24 ANN. REV. BANKING & FIN. L. 223, 227 (2005) (discussing notable corporate criminal scandals that have been uncovered in the wake of Enron); Mark Robeck et al., *supra* note 9, at 23 (“The fall of Enron was followed by the exposure of a disappointingly high number of other corporate scandals, leading to intense government and public scrutiny of corporate America.”).

30. Mary K. Rameriz, *The Science Fiction of Corporate Criminal Liability: Containing the Machine Through the Corporate Death Penalty*, 47 ARIZ. L. REV. 933, 956 (2005). Hints of a scandal at WorldCom began to surface in February 2002, when the company first reported that its fourth quarter profit for the previous year fell 64%. Floyd Norris, *MCI Chief Says He Repaid Debt, Borrowing from His Company*, N.Y. TIMES, Feb. 8, 2002, at C2. Bernard Ebbers, WorldCom's Chief Executive Officer and President, later admitted that he owed the company \$339.7 million on two loans. *Id.* Finally, in July, the company had to file for bankruptcy after it came to light that it had been improperly masking billions of dollars in losses as expenses. See Reuters, *WorldCom Restates Profits by \$74.4 Billion for 2 Years*, N.Y. TIMES, Mar. 13, 2004, at C14.

savings.<sup>31</sup> In the years immediately following the Enron and WorldCom revelations, criminally fraudulent activity at no less than nineteen other major U.S. corporations came to light, including Adelphia Communications, the nation's sixth largest provider of cable services; Rite Aid, a national drug store chain; Qwest Communications, the dominant provider of telephone service on the West Coast; and HealthSouth, the largest operator of rehabilitation medical centers in the country.<sup>32</sup> In total, corporate financial crimes in the first few years of this decade cost investors more than \$300 billion and tens of thousands of employees lost their jobs and retirement security.<sup>33</sup>

With the issue of corporate crime garnering massive media attention and drawing public outcry,<sup>34</sup> President Bush moved quickly in response.<sup>35</sup> In July 2002, the President established a Corporate

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31. Brook A. Masters & Amy Joyce, *Ebbers Starts 25-Year Term for Fraud at Worldcom*, WASH. POST, Sept. 27, 2006, at D1. Ebbers and Chief Financial Officer Scott Sullivan were both convicted of federal criminal offenses for their roles in the company's \$11 billion accounting fraud. *Id.* It was alleged by the government that Ebbers and Sullivan "jointly devised means to artificially inflate earnings to meet analysts' expectations" and made "misleading claims about the significant revenue growth and WorldCom's robust financial condition." Kathleen F. Brickey, *Symposium: White Collar Criminal Law in Comparative Perspective: The Sarbanes-Oxley Act of 2002: Enron's Legacy*, 8 BUFF. CRIM. L. REV. 221, 269–70 (2004) [hereinafter Brickey, *Symposium*]. Sullivan and WorldCom's Senior Vice President and Controller, David Meyers; Director of General Accounting, Buford Yates; Director of Management Reporting, Betty Vinson; and Director of Legal Entity Accounting, Troy Normand were also charged separately and pled guilty to conspiracy and securities fraud for their part in the scandal. *Id.* at 266–67. The fraud and resulting bankruptcy of WorldCom, the nation's second largest telecommunications company, wiped out an estimated 20,000 jobs. Masters & Joyce, *supra*.

32. See Brickey, *Symposium, supra* note 31, at 226–28, 247.

33. John Byrne, *Fall from Grace*, BUS. WK., Aug. 12, 2002, at 51.

34. A LexisNexis search yielded 7,242 articles concerning "corporate crime" published in major U.S. Newspapers in the eight months between Enron's bankruptcy announcement and the establishment of the Corporate Fraud Task Force. See, e.g., Amey Stone & Eric Wahlgren, *The Street's Death of a Thousand Cuts*, BUS. WK.ONLINE, Feb. 28, 2002 (Continuing corporate fraud "revelations [have] charred any remaining shred of confidence the . . . public has in the integrity of Corporate America."). A June 2002 Gallup Poll found that confidence in "Big Business" was at its lowest point in over twenty years. *Id.* A separate survey of jurors found that 62% "felt that their opinion of corporations had changed for the worse during 2002." Ed Aro et al., *How Juries and Judges are Reexamining Duties of Directors, Officers in Wake of Corporate Scandals*, 72 U.S.L.W. 2459 (Feb. 10, 2004).

35. "[O]ver the past year, high-profile acts of deception in corporate America have shaken people's trust in corporations, the markets, and the economy . . . The American people need to know we're acting. We're moving, and we're moving fast." Remarks at the Corporate Fraud

Fraud Task Force (“Task Force”).<sup>36</sup> The Task Force, chaired by the sitting Deputy Attorney General, was charged with providing direction for the investigation and prosecution of financial crimes committed by corporations and their employees.<sup>37</sup>

### C. The Thompson Memorandum

As part of the advancement of the Task Force’s mission, in January 2003, then Deputy Attorney General Larry Thompson authored a memorandum titled “Principles of Federal Prosecution of Business Organizations” (“Thompson Memo”).<sup>38</sup> Building on the Holder Memo,<sup>39</sup> the Thompson Memo laid out “a revised set of principles to guide [federal] prosecutors as they make the decision whether to seek charges against a business organization.”<sup>40</sup>

The main focus of the revisions is increased emphasis on and scrutiny of the authenticity of a corporation’s cooperation. Too

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Conference, 2 PUB. PAPERS 1665, 1665–66 (Sept. 26, 2002), available at <http://www.whitehouse.gov/news/releases/2002/09/20020926-10.html>.

36. Exec. Order No. 13,271, 3 C.F.R. 245 (2003) 091 (2002–2003), available at <http://www.whitehouse.gov/news/releases/2002/07/20020709-2.html>. Later that same month the President also signed into law the Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (2002). Notably, Titles VII and IX of the Act address “Corporate and Criminal Fraud Accountability” and “White-Collar Crime Penalty Enhancements” respectively. 18 U.S.C. §§ 1341, 1501 (Supp. II 2002). As President Bush noted when he signed the Act, “This law gives my administration new tools for enforcement. We will use them to the fullest.” Remarks on Signing the Sarbanes-Oxley Act of 2002, 2 PUB. PAPERS 1319, 1321 (July 30, 2002), available at <http://www.whitehouse.gov/news/releases/2002/07/20020730.html>. “[E]very dishonest corporate leader . . . will be exposed and punished.” *Id.* at 1319. For a comprehensive discussion of the Sarbanes-Oxley Act see, e.g., Brain Kim, *Sarbanes-Oxley Act*, 40 HARV. J. ON LEGIS. 235 (2003); Corey Braddock, Comment, *Penny Wise, Pound Foolish: Why Investors Would be Foolish to Pay a Penny or a Pound for the Protections Provided by Sarbanes-Oxley*, 2006 BYU L. REV. 175.

37. Exec. Order No. 13,271, 3 C.F.R. 245 (2002–2003). By “overseeing the investigation of corporate abusers and bringing them to account” the Task Force was to “function as a financial crimes SWAT team.” Remarks on Corporate Responsibility in New York City, 2 PUB. PAPERS 1194, 1196 (July 9, 2002), available at <http://www.whitehouse.gov/news/releases/2002/07/20020709-4.html>. For more detailed information about the Task Force, see USDOJ: DAG: Corporate Fraud Task Force, <http://www.usdoj.gov/dag/cftf/> (last visited Nov. 5, 2006).

38. Memorandum from Larry D. Thompson, Deputy Att’y Gen., to all U.S.D.O.J. Heads of Dep’t Components and U.S. Att’ys (Jan. 20, 2003) [hereinafter Thompson Memo] (on file with the U.S.D.O.J.), available at [http://www.usdoj.gov/dag/cftf/business\\_organizations.pdf](http://www.usdoj.gov/dag/cftf/business_organizations.pdf).

39. See Holder Memo, *supra* note 9.

40. Thompson Memo, *supra* note 38, introductory comment.

often business organizations, while purporting to cooperate with a Department investigation, in fact take steps to impede the quick and effective exposure of the complete scope of wrongdoing under investigation. The revisions make clear that such conduct should weigh in favor of a corporate prosecution.<sup>41</sup>

In substance, the Thompson Memo simply adopts, nearly word for word, the factors outlined in the Holder Memo.<sup>42</sup> True to its word, however, the Thompson Memo, unlike the Holder Memo, explicitly draws prosecutorial attention to “whether the corporation, while purporting to cooperate, has engaged in conduct that impedes the investigation.”<sup>43</sup> One other notable aspect is that, unlike the Holder Memorandum, the factors outlined in the Thompson Memorandum were binding on federal prosecutors.<sup>44</sup>

## II. REACTION TO THE THOMPSON MEMO

While the DOJ policy statements in the Holder Memo went largely unnoticed in the shadow of the Enron-era scandals,<sup>45</sup> the Thompson Memo’s solidification of those policies created a windfall

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41. *Id.*

42. *See* Finder, *supra* note 17, at 116. Indeed, the language used in the fourth factor of the Thompson Memo, concerning the corporation’s cooperation in the government investigation and its voluntary disclosure of wrongdoing, is carried over directly from the Holder Memo. *Compare* Holder Memo, *supra* note 9, § II.A.4 *with* Thompson Memo, *supra* note 38, § I.A.4. *But see* Thompson Memo, *supra* note 38, § II.A.8 (adding one new factor that was not explicit in the Holder Memo).

43. Thompson Memo, *supra* note 38, § VI.B. The Thompson Memo goes on to identify examples of such conduct, which include “overly broad assertions of corporate representation of employees or former employees.” *Id.*

44. *See* U.S. DEP’T OF JUSTICE, CRIMINAL RESOURCE MANUAL § 163 (2005), available at [http://www.usdoj.gov/usao/eousa/foia\\_reading\\_room/usam/title9/crm00163.htm](http://www.usdoj.gov/usao/eousa/foia_reading_room/usam/title9/crm00163.htm) (“The Thompson Memorandum sets forth nine factors that federal prosecutors *must* consider in determining whether to charge a corporation or other business organization.”) (emphasis added). *See also* Carmen Couden, Note, *The Thompson Memorandum: A Revised Solution or Just a Problem?*, 30 J. CORP. L. 405, 416 (2005) (“[C]orporations [should] consider the provisions set forth in the Thompson Memorandum as government ‘rules’ rather than discretionary ‘guidelines’ . . .”).

45. *See* Finder, *supra* note 17, at 115 (“Public sympathy for the legal rights of entities and their employees so profoundly affected by the Holder Memorandum was minimal or nonexistent as compared to the outrage expressed in favor of victims of corporate fraud and abuse.”).

of criticism, beginning in the private sector, and then moving to the judicial and legislative branches, which eventually evoked a response by the executive branch.

### A. The Private Sector

Opposition to the Thompson Memo began with criticism from not only the legal profession, but also from the business community and civil liberties organizations.<sup>46</sup> The vast majority of reform effort focused on protecting the perceived threat posed by the Thompson Memo to the attorney-client privilege.<sup>47</sup> However, the American Bar Association (“ABA”),<sup>48</sup> amongst others,<sup>49</sup> was an outspoken critic of

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46. An apt example of the “diverse and broadly representative constituency . . . all of whom are concerned by the governmental policies and practices” articulated in the Thompson Memo, is the Coalition to Preserve the Attorney-Client Privilege (“Coalition”). Submission to the Senate Judiciary Committee Regarding Hearings on Coerced Waiver of the Attorney-Client Privilege: The Negative Impact for Clients, Corporate Compliance, and the American Legal System (Sept. 12, 2006) [hereinafter Statement of the Coalition], available at <http://www.acc.com/public/attyclientpriv/coalitionsenjudtestimony.pdf>. The Coalition is comprised of, among other institutions, the American Chemistry Council, the American Civil Liberties Union, the National Association of Criminal Defense Lawyers, and the U.S. Chamber of Commerce. *Id.* Moreover, in September 2006, ten former Attorney Generals, Deputy Attorney Generals, and Solicitor Generals sent a joint letter to then-current U.S. Attorney General Alberto Gonzales expressing their concerns over the Thompson Memo policies and requesting reform. Letter from Griffin Bell et al., former Att’y Gen., to Alberto Gonzales, Att’y Gen. (Sept. 5, 2006), available at <http://www.acc.com/public/attyclientpriv/agsept52006.pdf>.

47. *See, e.g.*, Letter from Griffin Bell et al., *supra* note 46 (“[W]e urge the Department to revise its policy to state affirmatively that waiver of attorney-client privilege . . . should not be a factor in determining whether an organization has cooperated with the government in an investigation.”); Statement of the Coalition, *supra* note 46 (“Privilege waiver should not be . . . considered when assessing whether a corporation is cooperating in an investigation . . .”); THE DECLINE OF THE ATTORNEY-CLIENT PRIVILEGE IN THE CORPORATE CONTEXT, SURVEY RESULTS 3, COAL. TO PROTECT THE ATTORNEY-CLIENT PRIVILEGE (2006), available at <http://www.acc.com/Surveys/attyclient2.pdf> (noting that 75% of counsel who responded to the survey agree that a “culture of waiver” exists whereby the government expects a corporation under investigation to broadly waive its attorney-client privilege or work product protections).

48. The ABA, the national representative of the legal profession, provides “initiatives to improve the legal system for the public” and “promot[es] justice, professional excellence, and respect for the law.” About the American Bar Association, <http://www.abanet.org/about/> (last visited Jan. 15, 2007). In 2004, the ABA president created a new Presidential Task Force on the Attorney-Client Privilege. Press Release, AMERICAN BAR ASSOCIATION, ABA President Robert Grey Creates Task Force to Advocate for Attorney-Client Privilege (Oct. 6, 2004), available at <http://www.abanet.org/buslaw/attorneyclient/materials/pressrelease.pdf>.

49. For example, the Association of Corporate Counsel (“ACC”), which serves as the bar association for in-house corporate counsel, proposed a “redline” version of the Thompson Memo. *See* Association of Corporate Counsel, ACC Draft “Redline” of the Thompson

the Thompson Memo's direction to prosecutors that, in making their indictment decision, they consider whether a corporation has advanced legal fees to its employees.

To be sure, the ABA has called for the adoption of a government policy which uniformly bans permitting prosecutors, "in making a determination of whether an organization has been cooperative in the context of a government investigation" from taking into consideration "that the organization provided counsel to, or advanced, reimbursed or indemnified the legal fees and expenses of, an [e]mployee."<sup>50</sup> In support of its resolution, the ABA primarily asserts that the incentive of being deemed cooperative in the eyes of the government pressures corporations to refuse to pay the legal fees of their employees.<sup>51</sup> This in turn "denies individuals the benefits of representation."<sup>52</sup>

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Memorandum (Jan. 2006), <http://www.acc.com/resource/v7255> (follow "Research" tab; then follow "virtual library" hyperlink; search "redline"; follow "ACC Redline" of the Thompson Memo hyperlink). Among other changes, the ACC's version would require that the culpability of agents be proven before payment of their legal fees may be considered by prosecutors. *Id.* See also Lynnley Browning, *Judge Presses Companies that Cut Off Legal Fees*, N.Y. TIMES, Apr. 17, 2006, at C1 (quoting numerous sources criticizing the Thompson Memo's consideration of legal fees advancement).

50. AMERICAN BAR ASSOCIATION, TASK FORCE ON ATTORNEY-CLIENT PRIVILEGE, REPORT TO HOUSE OF DELEGATES, RECOMMENDATION ¶¶ 23-31 (2006), available at [http://www.abanet.org/buslaw/attorneyclient/materials/hod/emprights\\_recommendation\\_adopted.pdf](http://www.abanet.org/buslaw/attorneyclient/materials/hod/emprights_recommendation_adopted.pdf).

51. See R. William Ide, III, *Report to House of Delegates*, AMERICAN BAR ASSOCIATION TASK FORCE ON ATTORNEY-CLIENT PRIVILEGE (2006) [hereinafter ABA REPORT], [http://www.abanet.org/buslaw/attorneyclient/materials/hod/emprights\\_report\\_adopted.pdf](http://www.abanet.org/buslaw/attorneyclient/materials/hod/emprights_report_adopted.pdf). The ABA further argues that prosecutors sometimes encourage organizations to decide whether they will pay an employee's legal fees even before a determination of the employee's culpability in any wrongdoing has been established. *Id.* at 7.

52. ABA Report, *supra* note 51, at 9 ("Even for those Employees who can afford a lawyer, it will often be difficult if not impossible to afford a lawyer with the special expertise in white-collar criminal investigations and prosecutions and to finance the extensive legal work typically demanded to receive fully informed advice or to wage an effective defense to white-collar criminal allegations.").

*B. The Judicial Branch—United States v. Stein*<sup>53</sup>

The ABA's arguments, though largely ignored by the DOJ,<sup>54</sup> received affirmation by the Southern District of New York in *United States v. Stein*,<sup>55</sup> a case that seemed to typify the concerns that private sector critics had about the Thompson Memo. The facts of *Stein* revolved around a highly publicized investigation of KPMG LLP ("KPMG")<sup>56</sup> for developing and promoting allegedly illegal tax shelters.<sup>57</sup>

After catching word of the allegedly abusive tax shelters, the United States Senate Permanent Subcommittee on Investigations of the Committee on Governmental Affairs ("Subcommittee")<sup>58</sup> began

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53. 435 F. Supp. 2d 330 (S.D.N.Y. 2006).

54. In May 2006, ABA president Michael Greco sent a letter to Attorney General Alberto Gonzales urging him to modify the DOJ policy. Letter from Michael Greco, President, American Bar Association, to Alberto Gonzales, Att'y Gen. (May 2, 2006), available at [http://www.abanet.org/poladv/letters/attyclient/060502letter\\_acprivgonz.pdf](http://www.abanet.org/poladv/letters/attyclient/060502letter_acprivgonz.pdf). Although the DOJ responded to the letter, it simply restated its rationale for its current policy. See Letter from Crystal Jezierski, Director, Office of Intergovernmental and Public Liaison, U.S.D.O.J. to Michael Greco, President, American Bar Association (July 18, 2006), available at <http://www.abanet.org/poladv/priorities/acpriv/doj-ltr71806.pdf>.

55. 435 F. Supp. 2d 330 (S.D.N.Y. 2006). The presiding judge, Lewis Kaplan, also issued a companion opinion in the same case addressing other criticisms raised against the Thompson Memo. See discussion of *United States v. Stein*, 440 F. Supp. 2d 315 (S.D.N.Y. 2006) *infra* note 77.

56. KPMG is the United States' third largest accounting firm and generates more than \$4 billion in revenue annually. S. REP. NO. 109-54, at 11 (2005); see also KPMG INTERNATIONAL, KPMG Member Firms' Financial Performance (2005), <http://www.kpmg.com/NR/rdonlyres/869D922B-7431-4503-9007-26D2EA0FA86C/0/IAR2005FinancialPerformance.pdf>.

57. *United States v. Stein*, 435 F. Supp. 2d 330, 338 (S.D.N.Y. 2006). From 1998 through 2003 KPMG devoted a substantial amount of resources to developing and promoting "generic" tax products. S. REP. NO. 109-54, at 12. Unlike traditional tax strategies, which provide individualized tax advice to persons who initiate contact with a tax advisor, generic tax products are "aggressively marketed to multiple clients." *Id.* at 11. As the U.S. Senate Permanent Subcommittee on Investigations of the Committee on Governmental Affairs explains in its report on the topic, generic tax strategies that are widely marketed and not tailored to an individual customer can be problematic because:

In its broadest sense, the term "tax shelter" is a device used to reduce or eliminate the tax liability of the tax shelter user. This may encompass legitimate or illegitimate endeavors. While there is no one standard to determine the line between legitimate "tax planning" and "abusive tax shelters," the latter can be characterized as transactions in which a significant purpose is the avoidance or evasion of Federal, state or local tax in a manner not intended by law.

*Id.* at 1.

58. The Subcommittee's responsibilities include, investigating the "compliance or

an investigation into the tax shelter industry, culminating in two days of hearings in November 2003.<sup>59</sup> On the first day of the hearings six current and former KPMG employees testified.<sup>60</sup>

The result of the testimony was not favorable to KPMG.<sup>61</sup> Mark Watson, a former KPMG partner, acknowledged in his testimony that he believed at least one of KPMG's tax strategies was not in compliance with federal tax law.<sup>62</sup> Moreover, Jeffery Eischeid, a KPMG partner at the time, was admonished by Senator Levin for not giving straightforward answers to the Senator's questions.<sup>63</sup> Another partner, Philip Wiesner, reluctantly admitted that he was "bothered" by the actions that his firm had taken.<sup>64</sup> Finally, two tax experts testified that they believed KPMG's tax shelters violated federal tax laws.<sup>65</sup>

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noncompliance of . . . corporations . . . or other entities with the rules, regulations, and laws governing the various governmental agencies and their relationship with the public." Senate Committee on Homeland Security & Governmental Affairs, Committee on Homeland Security and Governmental Affairs Full Committee and Subcommittee Jurisdictions for the 109th Congress, <http://hsgac.senate.gov/index.cfm?Fuseaction=About.Jurisdiction> (follow "About the Committee" tab; then follow "Jurisdiction" hyperlink) (last visited Nov. 8, 2006).

59. S. REP. NO. 109-54, at 2.

60. Tax professionals testifying from KPMG included: Philip Wiesner, Partner in Charge, Washington National Tax Client Services; Jeffrey Eischeid, Partner, Personal Financial Planning; Lawrence DeLap, retired National Partner in Charge, Department of Professional Practice-Tax; Lawrence Manth, former West Area Partner in Charge, Stratecon; and Richard Smith Jr., Vice Chair, Tax Services. *Id.* Former KPMG partner Mark Watson also testified as a tax expert. *Id.*

61. At one point in the hearings Senator Coleman stated, "[A]nd I could spend a lot of time getting very angry, as my colleague, I think justifiably, so from Michigan [Senator Levin] has been as he has looked at the amounts of tax avoidance as a result of [KPMG's tax shelter] schemes and the impact it has." *U.S. Tax Shelter Industry: The Role of Accountants, Lawyers, and Financial Professionals: Hearing Before the Permanent Subcomm. on Investigations of the S. Governmental Affairs Comm.*, 108th Cong. 60 (2003) [hereinafter *Subcomm. Hearing*].

62. *See Subcomm. Hearing, supra* note 61, at 21.

63. In response to apparently evasive answers, Senator Levin instructed Eischeid, "Well try an honest answer. Just give me a direct answer to this." *Id.* at 43. To which Eischeid responded, "I'm trying my best, sir." *Id.* at 44. Senator Levin continued, "Why isn't that the straightforward answer?" *Id.*

64. Senator Levin asked Wiesner, "Are you troubled now when I tell you [KPMG] went ahead and sold [the tax strategy in question]? Does that bother you? Does anything bother you? Now I am asking you a direct question." *Id.* at 53. Unsatisfied with Wiesner's answer, Senator Levin again asked, "Could you answer my question?" *Id.* Still unsatisfied, Senator Levin requested for a third time, "Are you going to answer my question?" *Id.* Finally, Wiesner admitted, "Yes." *Id.*

65. *Id.* at 21 (testimony of Debra Peterson), 22 (testimony of Calvin Johnson).

Apparently concerned about the impact of the Subcommittee Hearing and a parallel investigation by the IRS,<sup>66</sup> KPMG decided to take a “cooperative approach,” which involved, among other things, the decision to “clean house” by terminating the employment of several senior level partners, including those who had testified before the Subcommittee.<sup>67</sup> Despite KPMG’s efforts to stave off trouble, in February 2005 the IRS made a criminal referral to the United States Attorney’s Office (“USAO”).<sup>68</sup> Within days of receiving the referral, the USAO issued subject letters to numerous KPMG employees.<sup>69</sup> At initial meetings with KPMG, prosecutors began expressing an interest in whether the firm had an obligation to pay the legal fees of its employees under investigation.<sup>70</sup> In an apparent effort to appease the government, KPMG advised its employees under investigation

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66. In 2002, the IRS served summonses on KPMG requesting records and testimony regarding certain company products. *See United States v. KPMG LLP*, 316 F. Supp. 2d 30, 32 (D.D.C. 2004).

67. *United States v. Stein*, 435 F. Supp. 2d 330, 339 (S.D.N.Y. 2006). Another partner asked to leave KPMG was Deputy Chair and CEO Jeffery Stein. *Id.* Stein’s departure was “cushioned substantially” with a severance package that included a \$100,000 per month, three-year consulting contract and an agreement to pay his legal fees for any subsequent suits that may be brought against him. *Id.*

68. *Id.* *See generally* BRICKEY, 3 CORPORATE LIABILITY, *supra* note 2, at 6 (“Criminal activity that goes well beyond civil or criminal tax violations thus may be discovered and referred [by the IRS] to the Justice Department.”). The USAO is the branch of the DOJ responsible for “[prosecuting] all offenses against the United States.” 28 U.S.C. § 547(1) (2000).

69. *Stein*, 435 F. Supp. 2d at 341. A subject letter is a “[letter] advising the recipient that he or she is a person whose conduct is within the scope of a grand jury investigation.” *Id.* In all, between twenty and thirty subject letters were issued to KPMG employees, including Stein, Watson, and Eischeid. *Id.*

70. *Id.* at 341–45. For example, at one meeting a prosecutor commented that under “federal guidelines” employee “misconduct” should not be rewarded. *Id.* at 342. There was substantial debate between the parties in pretrial proceedings regarding what the prosecutors meant by this. The government testified that it was trying to determine what type of severance agreements KPMG had entered with its terminated employees, and that by “federal guidelines” it was referring to the compliance provision under the Organizational Guidelines calling for discipline of employees who engage in misconduct. *Id.* at 342–43. *See supra* note 23 for a discussion of the Organizational Guidelines compliance provision. Thus, a substantial severance package would be a relevant consideration. *Stein*, 435 F. Supp. 2d at 344 n.51. Nonetheless, the court found that regardless of the government’s intent, given the contemporaneity of the legal fees inquiry and the misconduct statement, objectively it could have been perceived to imply that the payment of legal fees would be viewed as rewarding misconduct under the Thompson Memo. *Id.* at 342–44.

that it would voluntarily pay their legal expenses;<sup>71</sup> however, that payment would cease if the individual was indicted.<sup>72</sup>

The firm's efforts were successful. In August 2005, KPMG entered a Deferred Prosecution Agreement ("DPA") with the government, whereby the government agreed not to prosecute KPMG in exchange for, *inter alia*, KPMG's admission of wrongdoing, and full cooperation with any subsequent government investigation.<sup>73</sup> At approximately the same time, the government indicted numerous KPMG employees ("Defendants") for tax fraud.<sup>74</sup>

Pursuant to their agreement with the Defendants, KPMG ceased payment of their legal fees.<sup>75</sup> In response, the Defendants promptly moved to dismiss the indictment, arguing that the government had violated their constitutional rights by improperly interfering with the advancement of their legal fees by KPMG.<sup>76</sup> In a strongly worded opinion, the court agreed.<sup>77</sup>

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71. *Id.* at 345–46. KPMG capped the amount it would pay at \$400,000 per employee. *Id.* KPMG further conditioned the legal fees payment upon the individual's full cooperation with the government. *Id.* at 345–46.

72. *Id.* KPMG stipulated that although not mandated by state law or explicit in its partnership agreement, "it had been the longstanding voluntary practice of KPMG to advance and pay the legal fees [of its employees], without a present cap or condition of cooperation with the government" where criminal or civil charges were brought against the individual "involving activities arising within the scope of the individual's [employment]." *Id.* at 340. KPMG also stipulated however, that it was not aware of any KPMG partners or employees who had been indicted for conduct arising within the scope of employment since 1974, when two partners were indicted. *Id.* With regard to the 1974 indictments, although KPMG had no records showing payment of the partners' legal fees, it believed that the fees were paid by KPMG. *Id.*

73. *Id.* at 349. The terms of the DPA actually call for KPMG to be charged with a one-count information. *Id.* The government agreed to seek dismissal of the information if KPMG complied with the provisions of the DPA. *Id.* For a complete copy of the DPA, see Memorandum from David Kelley, U.S. Attorney, Southern District of N.Y., to Robert Bennett, Skadden, Arps, Slate, Meagher, & Flom LLP (Aug. 26, 2005), available at <http://www.usdoj.gov/usao/nys/pressreleases/August05/kpmgdpagmt.pdf>.

74. See *Stein*, 435 F. Supp. 2d at 350; see also Press Release, Department of Justice, KPMG to Pay \$456 Million for Criminal Violations in Relation to Largest-Ever Tax Shelter Fraud Case (Aug. 29, 2005), available at [http://www.usdoj.gov/opa/pr/2005/August/05\\_ag\\_433.html](http://www.usdoj.gov/opa/pr/2005/August/05_ag_433.html). The government later filed a superseding indictment naming nineteen defendants, almost all of whom were KPMG employees. Press Release, Dep't of Justice, 19 Individuals Charged in Superseding Indictment Filed in Criminal Tax Case Related To KPMG Tax Shelters (Oct. 17, 2005), available at <http://www.usdoj.gov/usao/nys/pressreleases/October05/kpmgsupersedingindictmentpr.pdf>.

75. *Stein*, 435 F. Supp. 2d at 350.

76. *Id.*

77. See generally *Stein*, 435 F. Supp. 2d 330. Throughout the opinion the court harshly

First, the court held that the government had violated the Defendants' Fifth Amendment<sup>78</sup> right to fairness in the criminal process.<sup>79</sup> The court reached this conclusion by first finding that the right to "obtain and use in order to prepare a defense resources lawfully available to [a defendant], free of knowing or reckless government interference" is a "fundamental" right.<sup>80</sup> Next, the court concluded that the Thompson Memo impinged on this fundamental right.<sup>81</sup> This is so, the court reasoned, because the Thompson Memo interfered with the ability of the Defendants to obtain resources to defend themselves that they otherwise would have had.<sup>82</sup> Consequently, the court opined that the Thompson Memo and the government's actions thereunder were subject to strict scrutiny.<sup>83</sup>

Applying the strict scrutiny standard, the court found that the Thompson Memo was not the least restrictive alternative to achieve a compelling government interest.<sup>84</sup> In that regard, the court reasoned that although "[a]ny government's interest in investigating and fairly

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criticizes the USAO's actions in implementing the Thomson Memo. *See, e.g., id.* at 336 ("The government . . . has let its zeal get in the way of its judgment. It has violated the Constitution it is sworn to defend.")

In a companion opinion Judge Kaplan also holds that the Thompson Memo improperly interfered with certain Defendants Fifth Amendment right against making self incriminating statements. *See United States v. Stein*, 440 F. Supp. 2d 315, 331–33, 337 (citing U.S. CONST. amend. V). In that case the court opined that, in an effort to be viewed as "cooperative" under the Thompson Memo guidelines, KPMG's threats to terminate the Defendants' employment, or cut off payment of their legal fees, impermissibly compelled the Defendants to make self incriminating statements to the government. *Id.* at 334–35.

78. U.S. CONST. amend. V.

79. *Stein*, 435 F. Supp. 2d at 362. The right to fairness in the criminal process is protected by the Due Process Clause of the Fifth Amendment. *Id.* at 357.

80. *Id.* at 361–62.

81. *Id.* at 362.

82. *Id.* Previously in the opinion, the court concluded that the language of the Thompson Memo implied that a corporation's payment of legal fees to indicted employees would be held against the corporation. *Id.* at 352–53. And that "absent the Thompson Memo . . . KPMG would have paid the legal fees" of its employees both prior to and after indictment, consistent with "its long-standing policy of paying legal fees" of its employees "in all cases." *Id.* at 353, 352. *But cf. supra* note 72 for a discussion of KPMG's history of paying its employees' legal fees.

83. *United States v. Stein*, 435 F. Supp. 2d 330, 362 (S.D.N.Y. 2006). The strict scrutiny test requires that the government's purpose for impingement on fundamental rights be "legitimate" or "compelling" and the means employed to achieve that purpose be "necessary" or the "least restrictive alternative." *See ERWIN CHERMERINSKY, CONSTITUTIONAL LAW PRINCIPLES AND POLICIES* 520 (2d ed. 2002).

84. *Stein*, 435 F. Supp. 2d at 364.

prosecuting crime is compelling . . . the Thompson Memorandum does not say that payment of legal fees may cut in favor of indictment *only if* it is used as a means to obstruct an investigation.”<sup>85</sup> Therefore, the court held, the Thompson Memo “burdens excessively the constitutional rights of the individuals whose ability to defend themselves it impairs” and, accordingly, violates the Fifth Amendment.<sup>86</sup>

Second, the court held that the Thompson Memo, and the government’s implementation, violated the Defendants’ Sixth Amendment right to counsel.<sup>87</sup> This was so, according to the court, because “[t]he Thompson Memorandum discourages and, as a practical matter, often prevents companies from providing employees . . . with the financial means to exercise their constitutional rights to defend themselves.”<sup>88</sup> The court reasoned, “[T]hat advancement of legal fees might occasionally be part of an obstruction scheme or indicate a lack of full cooperation . . . is insufficient to justify the government’s interference with the right of individual criminal defendants to obtain resources lawfully available to them in order to defend themselves . . . .”<sup>89</sup>

Yet, despite the court’s pointed language admonishing the Thompson Memo, it initially refused to dismiss the indictment or order either the government or KPMG to advance the Defendants’ legal fees.<sup>90</sup> Instead, the court invited the Defendants to bring a civil suit against KPMG to compel the firm to fund their defense and ordered the criminal proceedings stayed pending the outcome of the civil suit.<sup>91</sup> Only after the Second Circuit Court of Appeals dismissed the Defendants’ civil suit against KPMG, holding that an ancillary

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85. *Id.* at 363.

86. *Id.* at 364.

87. *Id.* at 367 (citing U.S. CONST. AMEND. VI).

88. *Id.* at 368.

89. *Id.* at 369.

90. *Stein*, 435 F. Supp. 2d at 374, 376, 380.

91. *Id.* at 380. Pursuant to the court’s suggestion, in July 2006, the Defendants filed a complaint against KPMG for advancement of their defense costs. Complaint for Advancement, *Stein v. KPMG LLP*, No. 1:06-cv-5007-LAK, 2006 WL 2922089 (S.D.N.Y. July 10, 2006). Interestingly, despite the court’s holding against government interference with the Defendants’ access to legal fees, it urged the government to use its “substantial influence” and “power to cause KMPG to advance the defense costs.” *Stein*, 435 F. Supp. 2d at 380.

civil proceeding was not the proper remedy,<sup>92</sup> did the *Stein* court, in a later opinion, dismiss the criminal indictments against the majority of the Defendants.<sup>93</sup>

### C. The Legislative Branch

Shortly after the *Stein* opinion came down, and perhaps in response thereto, Congress joined the attack on the Thompson Memo. In September 2006, the Senate Judiciary Committee (“Committee”) held a hearing to discuss the effects of the Thompson Memo.<sup>94</sup> At the hearing, Senators, institutional advocates, and corporate defenses lawyers testified, eschewing harsh criticism of the Thompson Memo.<sup>95</sup>

The Chair of the Committee, Senator Arlen Specter, began the proceeding by bluntly stating that the Thompson Memo’s “consideration of the, ‘Value of a corporation’s cooperation,’ in charging [decisions] . . . is coercive. [I]t even rise[s] to the level of being obliging.”<sup>96</sup> Moreover, in an apparent reference to the *Stein* holding,<sup>97</sup> Senator Specter opined, “I do not think somebody ought to get credit for waiving a constitutional right, or ought to get . . . a demerit or a deficit for asserting a constitutional right.”<sup>98</sup> Senator

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92. *Stein v. KPMG*, 486 F.3d 753 (2d. Cir. 2007). The Second Circuit held that even if there were constitutional violations, “more direct (and far less cumbersome) remedies are available.” *Id.* at 763. Namely, the court stated that dismissal of the indictment, allowing the Defendants to seek post-conviction relief, or ordering cessation of the constitutionally offensive conduct were the proper remedies available to the *Stein* court. *Id.* Notably, however, the Second Circuit refrained from addressing the merits of the *Stein* decision. *Id.* at 756.

93. *United States v. Stein*, No. S1 05 Crim. 0888, 495 F. Supp. 2d 390 (S.D.N.Y. July 16, 2007). The court ordered the criminal indictments to be dismissed against all but three of the former KPMG employees. *Id.* at 394. Two of the three former employees whose indictments were not dismissed had left KPMG before they engaged in the conduct for which they were indicted. *Id.* The third former employee whose indictment was not dismissed had signed a release, before leaving the firm, releasing KPMG from all contractual liabilities. *Id.* at 426.

94. *The Thompson Memorandum’s Effect on the Right to Counsel in Corporate Investigations: Hearing Before the S. Comm. on the Judiciary*, 109th Cong. (forthcoming 2007), available at Fed. News Service (Sept. 12, 2006) (Lexis) [hereinafter *Comm. Hearing*].

95. See Lynnley Browning, *Justice Department Is Reviewing Corporate Prosecution Guidelines*, N.Y. TIMES, Sept. 13, 2006, at C3.

96. *Comm. Hearing*, *supra* note 94, at \*10.

97. See *supra* notes 79, 87 and accompanying text.

98. *Comm. Hearing*, *supra* note 94, at \*11.

Specter went on to ask Deputy Attorney General Paul McNulty, who was testifying at the hearing, to reconsider the policy.<sup>99</sup>

Despite the Senator's request and McNulty's pledge to "consider all possibilities,"<sup>100</sup> on December 8, 2006, Senator Specter introduced legislation that effectively spelled the end of the Thompson Memo.<sup>101</sup> The bill, whose stated purpose is "to place on each agency clear and practical limits designed to . . . preserve the constitutional rights and other legal protections available to employees," in relevant part provides:

[A]n agent or attorney of the United States shall not . . . condition a civil or criminal charging decision relating to an organization . . . on, or use as a factor in determining whether an organization . . . is cooperating with the Government . . . the provision of counsel to, or contribution to the legal defense fees or expenses of, an employee of that organization."<sup>102</sup>

#### *D. The Executive Branch*

Despite executive branch officials' satisfaction with the state of corporate prosecutions under the Thompson Memo,<sup>103</sup> less than a

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99. *Id.* at \*10.

100. *See id.*

101. Attorney-Client Privilege Protection Act of 2006, S. 30, 109th Cong. (2006). *See also* John J. Carney & Dennis O. Cohen, *McNulty Memo: Changes Game or Keeps Congress Out?*, 237 N.Y.L.J. 4 (2007) ("In what may have been a high stakes game of chicken, Senator Arlen Specter" introduced a bill "that would completely moot many of the hotly contested issues raised by the Thompson Memorandum."). An identical version of the bill was re-introduced by Senator Specter at the beginning of the 2007 term. *See* Attorney-Client Privilege Protection Act of 2007, S. 186, 110th Cong. (2007).

102. S. 186, The 110th Cong. (2007) (referred to the S. Comm. on the Judiciary Jan. 4, 2007) The language of the bill coincides with suggestions given by other witnesses testifying at the Committee hearing. *See, e.g., Comm. Hearing, supra* note 94, at \*15 (testimony of Edwin Meese, former Att'y Gen.) ("I think that all reference in the memorandum to a company's payment of its employees' legal fees . . . should be eliminated."); *id.* at \*19 (testimony of Karen Mathis, President, Am. Bar Ass'n) ("The ABA urges the committee to encourage the Justice Department to eliminate these employee-related provisions from the Thompson Memorandum."). The bill has been referred to the Senate Judiciary Committee for consideration. 153 CONG. REC. S41 (daily ed. Jan. 4, 2007).

103. *See, e.g.,* CORP. FRAUD TASK FORCE, SECOND YEAR REPORT TO THE PRESIDENT (2004), available at [http://www.usdoj.gov/dag/cftf/2nd\\_yr\\_fraud\\_report.pdf](http://www.usdoj.gov/dag/cftf/2nd_yr_fraud_report.pdf). ("[W]e have met the President's charge—we are cleaning up corporate board rooms . . . and importantly, the

week after Senator Specter introduced his bill, the DOJ caved to the mounting pressure. On December 12, 2006, Deputy Attorney General Paul McNulty introduced new guidelines to supersede the Thompson Memo ("McNulty Memo").<sup>104</sup> The McNulty Memo carries over the same factors outlined by the Thompson Memo, including the much criticized fourth factor which focuses prosecutors' attention on the "corporation's willingness to cooperate in the investigation of its agents."<sup>105</sup>

Notwithstanding its lip service to the Thompson Memo,<sup>106</sup> however, the McNulty Memo puts bright-line limits on "[r]elevant considerations in determining whether a corporation has cooperated."<sup>107</sup> Namely, the McNulty Memo provides that "[p]rosecutors generally *should not* take into account whether a corporation is advancing attorneys' fees to employees or agents under investigation".<sup>108</sup> Instead, the memo asserts that only "[i]n extremely

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confidence of the American public in the integrity of our financial markets is returning. . . ."); Paul McNulty, Deputy Attorney General, Let's Make a Deal: The Question of Privilege (Sept. 13, 2006), *available at* [http://www.usdoj.gov/dag/speech/2006/dag\\_speech\\_060913.htm](http://www.usdoj.gov/dag/speech/2006/dag_speech_060913.htm) ("The analysis in the Thompson Memo is transparent, simple, and relies on the common sense approach prosecutors have been using for decades.").

104. Memorandum from Paul McNulty, Deputy Attorney General, to all U.S.D.O.J. Heads of Department Components and U.S. Attorneys (2006) [hereinafter McNulty Memo] (on file with the U.S.D.O.J.), *available at* [http://www.lawprofessors.typepad.com/whiecollarcrime\\_blog/files/mcnulty-memo.pdf](http://www.lawprofessors.typepad.com/whiecollarcrime_blog/files/mcnulty-memo.pdf); Paul McNulty, Deputy Attorney General, Prepared Remarks of Deputy Attorney General Paul J. McNulty at the Lawyers for Civil Justice Membership Conference Regarding the Department's Charging Guidelines in Corporate Fraud Prosecutions (Dec. 12, 2006) [hereinafter McNulty remarks], *available at* [http://www.usdoj.gov/dag/speech/2006/dag\\_speech\\_061212.htm](http://www.usdoj.gov/dag/speech/2006/dag_speech_061212.htm).

105. *Compare* McNulty Memo, *supra* note 104, § III.A with Thompson Memo, *supra* note 38, § II.A.

106. *See, e.g.*, McNulty Memo, *supra* note 104, at introductory cmt. ("I remain convinced that the fundamental principles that have guided our enforcement practices are sound."); McNulty Remarks, *supra* note 104 ("The new memorandum clarifies the intent of the Thompson Memorandum.").

107. McNulty Memo, *supra* note 104, § VII.B.

108. *Id.* § VII.B.3 (emphasis added). This guidance is in direct contrast to the Thompson Memo's provision that "a corporation's promise of support to culpable employees . . . through the advancing of attorneys fees . . . may be considered by prosecutors in weighing the extent and value of a corporation's cooperation." Thompson Memo, *supra* note 38, § VI.B. The McNulty Memo also significantly changes the circumstances in which prosecutors may request waiver of a corporation's attorney-client privilege. *See* McNulty Memo, *supra* note 104, § VII.B.2. For an in-depth discussion of the McNulty Memo's revision to prosecutorial privilege waiver policies see Thomas C. Frongillo & Elisa Jaclyn, *DOJ's Revision of its Charging Guidelines in Corporate Prosecutions*, in 21 ANDREWS WHITE-COLLAR CRIME

rare cases,” may the advancement of attorneys’ fees be taken into account.<sup>109</sup> When such “rare cases” arise, approval must be sought from the Deputy Attorney General.<sup>110</sup> Ironically, McNulty’s softening of the Thompson Memo came the very day that Jeffrey Skilling, the last of the major players in the Enron scandal, was ordered to begin serving a twenty-four year sentence for his role in the fraud that sparked the drafting of the Thompson Memo.<sup>111</sup>

### III. HAS THE PROBLEM BEEN SOLVED?

#### A. Preliminary Matters

Before we ask whether the solutions proposed by the judiciary or Congress, or the one adopted by the DOJ, provide a successful resolution to the criticisms lodged against prosecutors’ consideration of legal fees advancement, it is instructional to further examine the underlying premises of the critics’ positions.

#### 1. Possibility of Coercion

There is little doubt that a criminal indictment can have devastating effects on a corporation. This is especially true where the entity’s business is almost entirely dependant on its reputation. In the financial services industry in which KPMG is engaged, an indictment can, and has, been “tantamount to a death sentence.”<sup>112</sup> Consequently, it can be argued that anything the government may consider, which lessens the chance of indictment is “coercive” in that companies have a massive financial incentive to avoid indictment.<sup>113</sup> Flatly enforcing

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REPORTER no.5, at 2 (2007).

109. McNulty Memo, *supra* note 104, § VII.B.3 n.3.

110. *Id.*

111. See Associated Press, *Skilling Is Denied Bail*, N.Y. TIMES, Dec. 12, 2006, at C3.

112. Kathleen F. Brickley, *Anderson’s Fall from Grace*, 81 WASH. U. L.Q. 917, 921 (2003). See also Samuel W. Buell, *The Blaming Function of Entity Criminal Liability*, 81 IND. L.J. 473, 487–88 (2005) [hereinafter Buell, *The Blaming Function*] (discussing a firm’s reputation as its “capital, and the vulnerability of that capital in the criminal process”).

113. Cf. Written Testimony from Andrew Weissman, Former Assistant U.S. Attorney, Before the United States Senate Committee on the Judiciary Concerning the Thompson Memorandum’s Effect on the Right to Counsel in Corporate Investigations (Sept. 12, 2006), available at <http://www.acc.com/public/attyclientpriv/weissmann.pdf> (“The current standard for

the law, however, by removing opportunities for a target corporation to earn leniency would certainly not be a more desirable alternative from the corporation's standpoint.<sup>114</sup>

Rather than removing incentives, a more fruitful analysis is to focus on the federal system of enterprise criminal liability.<sup>115</sup> Under the United States' current *respondeat superior* regime of corporate criminal liability, it is quite easy, especially with large corporations, to impute criminal liability onto an employer.<sup>116</sup> Virtually all the doctrine requires is the wrongdoing of one low-level agent.<sup>117</sup> Therefore, although the factors prosecutors consider when determining whether to grant leniency may have a coercive effect, eliminating those factors altogether is a misguided remedy. To ameliorate the negative effects of the power prosecutors carry, efforts should instead focus on examining alternatives or modifications to the current system of corporate criminal liability.<sup>118</sup>

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corporate criminal responsibility affords prosecutors enormous—and unduly disproportionate—leverage and power.”).

114. As McNulty observed in his prepared statement submitted at the Committee Hearing, “The irony of the attacks on the Thompson Memo is that the federal criminal justice system would be a much harsher, less predictable, and less transparent environment for corporations and their counsel in the absence of this guidance.” Statement, Paul McNulty, Deputy Attorney General, Before the United States Senate Committee on the Judiciary Concerning the Thompson Memorandum’s Effect on the Right to Counsel in Corporate Investigations (Sept. 12, 2006), available at <http://www.acc.com/resource/getfile.php?id=7554>.

115. See generally Buell, *The Blaming Function*, *supra* note 112, at 478 (arguing for a more limited scope of entity criminal liability to “make the doctrine fit better with its justifications”).

116. See BRICKEY, CORPORATE LIABILITY, *supra* note 2, at 8–11. Under Federal law, a corporation is criminally responsible for the acts of its employees, so long as they are committed within the scope of employment and, at least in part, for the benefit of the employer. See, e.g., *United States v. Potter*, 463 F.3d 9, 25 (1st Cir. 2006); *United States v. Jorgenson*, 144 F.3d 550, 560 (8th Cir. 1998); *Mylan Lab., Inc. v. Akzo*, 2 F.3d 56, 63 (4th Cir. 1993).

117. See Buell, *The Blaming Function*, *supra* note 112, at 526 (“[T]he law says firms are virtually always answerable for their agents’ crimes, almost without regard to the facts.”).

118. See John Hasnas, *Do Nothing*, WALL ST. J., Sept. 16, 2006, at A9 (“Attempting to reform DOJ policy without changing the . . . untenable standard of corporate criminal liability . . . law is a bit like treating a lung-cancer patient’s cough. . . it won’t hurt, but it won’t help that much either.”); Andrew Weismann and David Newman, *Rethinking Criminal Corporate Liability*, 82 IND. L.J. 412, 425 (2007) (The willingness of corporations to cooperate with the government “is due in large measure to the vastly disproportionate power of the two sides. Prosecutors have enormous leverage due to the doctrine of vicarious liability.”). See also Buell, *The Blaming Function*, *supra* note 112, at 474–77, 527–37 for a discussion of numerous proposed reformations to corporate criminal liability.

## 2. Cooperation as an Appropriate Consideration

From a historical context, a defendant's willingness to cooperate has long been used in individual prosecutorial and sentencing decisions.<sup>119</sup> It is likely that this consideration comes from the socially accepted view that admission of guilt and acceptance of wrongdoing is praiseworthy.<sup>120</sup> Moreover, as a practical matter, when an entity learns that it is under government scrutiny, it is standard practice to begin an internal investigation.<sup>121</sup> Indeed, some corporations expend huge sums of money hiring outside counsel to review documents, conduct employee interviews, and provide opinions on the source and extent of any wrongdoing.<sup>122</sup> Counsel will then likely present their findings to the government to make an argument about why the corporation should not be indicted.<sup>123</sup> Given the amount of resources expended, even if cooperation was not an explicit factor in the prosecutor's decision, the company would likely expect leniency, in any event, for its efforts.<sup>124</sup> Additionally, to require expenditure of government resources to duplicate an investigation that a corporation has already completed, and is willing to share with the government, would be grossly inefficient and in some instances not feasible.<sup>125</sup> Thus, providing the target corporation with an incentive to cooperate via a credit in the indictment decision serves the interests of both the target corporation and the government.

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119. See U.S. SENTENCING GUIDELINES MANUAL § 3E1.1 (2004); *supra* notes 18, 22–24 and accompanying text.

120. By cooperating with the government, firms hope to “dampen [the] reputation effects” of an investigation because the public recognizes that “acceptance of responsibility . . . is essential to the credibility” of the firm. Buell, *The Blaming Function*, *supra* note 112, at 507.

121. See generally Kestenbaum & Criss, *supra* note 11, at 151–52 (cataloging the benefits a company reaps, and the risks it avoids, by conducting internal investigations).

122. See Robeck et al., *supra* note 9, at 25–26 (discussing the general process of internal investigations).

123. See Kestenbaum & Criss, *supra* note 11, at 151–52.

124. See *Comm. Hearing*, *supra* note 94, at 6–8 (testimony of Paul McNulty, Deputy Attorney General).

125. See *Interview with United States Attorney James B. Comey Regarding the Department of Justice's Policy on Requesting Corporations under Criminal Investigation to Waive the Attorney Client Privilege and Work Product Protection*, 51 U.S. ATT'YS' BULL., Nov. 2003, at 3–4, available at [http://www.usdoj.gov/usao/eousa/foia\\_reading\\_room/usab5106.pdf](http://www.usdoj.gov/usao/eousa/foia_reading_room/usab5106.pdf).

### 3. The Relevancy of Advancing Legal Fees

It is important to remember that, although corporations are considered legal entities under the law, the only way that they can act is through their agents.<sup>126</sup> When a corporation admits wrongdoing, the underlying admission is that one or more of its employees have engaged in wrongdoing.<sup>127</sup> Accordingly, it is contrary to the very idea of cooperation if the corporation seeks leniency by admitting wrongdoing and pledges to root out the wrongdoers, yet in actuality attempts to shield the culpable employees from liability by voluntarily paying their defense fees without any legal or contractual impetus.<sup>128</sup> Indeed, the court in *Stein* admitted as much<sup>129</sup> and drew an analogy to the Watergate case, in which the legal fees of the individuals who broke into the offices of the Democratic National Committee were paid “to buy the silence of the [wrongdoers] and to protect higher-ups.”<sup>130</sup> Corporate equivalents, the *Stein* court observed, “no doubt occur.”<sup>131</sup>

The relevancy issue notwithstanding, a primary criticism of factoring the advancement of employee legal fees into corporate indictment decisions is the application of this consideration before a finding of employee culpability has been made.<sup>132</sup> The *Stein* court and others have rightly observed, “The imposition of economic

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126. See BRICKEY, CORPORATE LIABILITY, *supra* note 2, at 89.

127. *Id.* at 89–90.

128. Significantly, throughout the evolution of DOJ policy, as articulated by the Holder, Thompson, and McNulty Memos, the advancement of legal fees has consistently been only one factor in determining whether the entity is in fact cooperating, which itself is only one factor among many that prosecutors are instructed to consider in making indictment decisions. See *supra* note 14 and text accompanying notes 42, 105. Similarly, DOJ policy has recognized that where state or contractual law places legal obligations on employers to indemnify employees, payment of employee legal fees may not be considered by prosecutors. See McNulty Memo, *supra* note 104, § VII.B.3. For example, organizations incorporated in Delaware are mandated to pay the legal fees of their employees who are successful on the merits of a criminal or civil action brought against them. DEL CODE ANN. tit. 8, § 145(c) (2001). In such instances, indemnification may not weigh into prosecutorial decisions.

129. *United States v. Stein*, 435 F. Supp. 2d 330, 363 (S.D.N.Y. 2006) (“[No one] suggest[s] that an entity’s obstruction of a government investigation . . . should be ignored in a charging decision.”).

130. *Id.*

131. *Id.*

132. See *supra* note 51 and text accompanying note 85.

punishment by prosecutors, before anyone has been found guilty of anything, is not a legitimate governmental interest . . . .”<sup>133</sup> However, the solutions that have been proposed by the judicial, legislative, and executive branches<sup>134</sup> to curb illegitimate application of this factor fall well short of the mark.

### *B. The Judicial Resolution is Inadequate*

*Stein* attempted to use the Constitution to rein in the government.<sup>135</sup> One commentator has exposed this solution as a “red herring.”<sup>136</sup> What’s more, subsequent courts have found ways to distinguish *Stein*<sup>137</sup> or have flatly refused to follow the precedent, finding the reasoning “unpersuasive.”<sup>138</sup> Regardless of how it is characterized, the court’s solution fails on a number of grounds.

The court goes through excruciating efforts to craft a finding that a defendant’s right to use “available resources” for his or her defense, free from government interference, is a “fundamental right” protected by the Fifth Amendment.<sup>139</sup> In reaching this holding, however, *Stein* primarily draws on *dicta* from other courts.<sup>140</sup> Indeed, the court admits that this right “has not been explicitly so characterized by the [Supreme] Court.”<sup>141</sup> The Supreme Court has, in fact, reserved the label of “fundamental right” for only those rights that are “deeply rooted in this nation’s history and tradition and implicit in the

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133. *Stein*, 435 F. Supp. 2d at 363.

134. See discussion *supra* Part II.B–D.

135. See *supra* text accompanying notes 79–90.

136. See Samuel W. Buell, *Criminal Procedure Within the Firm*, 59 STAN. L. REV. 1613, 1659 (2007) [hereinafter Buell, *Criminal Procedure*].

137. See, e.g., U.S. v. Galante, No. 3:06CR161 (EBB), slip op. at 3 (D. Conn. Nov. 28, 2006) (distinguishing United States v. Stein, 435 F. Supp. 2d 330 (S.D.N.Y. 2006) on the facts).

138. See U.S. v. Stodder, No. 2:05-CR-00027, 2006 WL 3066196, at \*2 (C.D. Cal. Oct. 4, 2006) (“[T]he *Stein* decision [is] scholarly but ultimately unpersuasive” because of “no support for [its holding] in the Supreme Court decisions cited in *Stein* or in any appellate court decisions.”). *But see* United States v. Payment Processing Ctr., LLC, 439 F. Supp. 2d 435, 439 (E.D. Pa. 2006) (citing favorably United States v. Stein, 435 F. Supp. 2d 330, 349–53 (S.D.N.Y. 2006)).

139. United States v. Stein, 435 F. Supp. 2d 330, 361–62 (S.D.N.Y. 2006). To reach this legal conclusion the court’s reasoning spans seven pages of the reporter. See *id.* at 356–63.

140. See *id.* at 361.

141. *Id.* at 360.

concept of ordered liberty.”<sup>142</sup> Examples of recognized fundamental rights, which include the right to vote,<sup>143</sup> freedom of speech,<sup>144</sup> and the right to privacy,<sup>145</sup> are limited and do not seem at all analogous to an expectation to be indemnified by one's employer for potentially criminal activity.<sup>146</sup> *Stein's* characterization of the right as “fundamental” is crucial to its holding because that is the only way the court can examine the Thompson Memo under strict scrutiny.<sup>147</sup> Without applying a strict scrutiny test, the government's action under the Thompson Memo is much more likely to be upheld.<sup>148</sup>

The court's Sixth Amendment argument is also problematic. Assuming *arguendo* that the court was correct in its novel finding that employees have a “property” interest in the expectation, even absent a statutory or contractual mandate, in their legal fees being paid by their employer,<sup>149</sup> the true detriment of relying on the Sixth Amendment as a solution is that it has a limited application. An individual's Sixth Amendment right to counsel does not attach until the government has initiated adversarial judicial criminal proceedings against the individual.<sup>150</sup> Therefore, in situations where a corporation preemptively refuses to pay the legal fees of an employee under investigation, in order to curry government favor, the Sixth

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142. *Chavez v. Martinez*, 538 U.S. 760, 775 (2003) (internal citations omitted).

143. *See Kramer v. Union Free Sch. Dist.*, 395 U.S. 621, 626 (1969).

144. *See McIntyre v. Ohio Elections Comm'n*, 514 U.S. 334, 336 n.1 (1995).

145. *See Planned Parenthood of Se. Pa. v. Casey*, 505 U.S. 833, 926–27 (1992).

146. Indeed, when conducting its Sixth Amendment analysis later in the opinion, the court draws a closer analogy between the Defendants' “right” to legal fees advancement and a property right. *U.S. v. Stein*, 435 F. Supp. 2d 330, 367 (S.D.N.Y. 2006); *see also infra* note 149 and accompanying text for further discussion on this point.

147. The most intensive kind of judicial scrutiny, strict scrutiny, is only used when courts evaluate discrimination based on national origin or for interference with fundamental rights. *See CHEMERINSKY, supra* note 83, at 520.

148. “The level of scrutiny used [by a court] is very likely to determine the outcome. If rational basis review is applied, the law is likely to be upheld. If strict scrutiny is used, the law is likely to be struck down.” *Id.*

149. *Stein*, 435 F. Supp. 2d at 367 (2006) (Defendants' expectation that their legal fees would be paid by KPMG “and any benefits that would have flowed from that expectation—the legal fees at issue now—were, in every material sense, their property.”).

150. *U.S. v. Gouveia*, 467 U.S. 180, 189 (1984). Although the right to counsel may attach for “critical pretrial proceedings,” the government must first have “committed itself to prosecute.” (internal quotations omitted) *Id.*

Amendment would afford no protection to that employee until after he or she has been indicted.

Although this was not the situation with the KPMG Defendants, it is certainly plausible that such situations can, and do, arise. There are a myriad of investigative techniques that prosecutors employ before an indictment decision is made, where employees would be well advised to have the assistance of counsel.<sup>151</sup> Thus, from the standpoint of crafting a resolution that sets forth clear guidelines that that can be broadly applied, relying on the protections afforded by the Sixth Amendment fails.

### *C. The Legislative Branch's Resolution is Inadequate*

Congress, as well as many advocates in the private sector, proposes completely eliminating advancement of employees' legal fees from prosecutorial consideration.<sup>152</sup> This solution is clearly a case of throwing out the baby with the bathwater. It altogether ignores that such activity can in fact be used to impede enforcement objectives<sup>153</sup> and gives the misguided impression that such conduct does not, or will not, occur.<sup>154</sup>

Much of Senator Specter's criticism is based on the premise that there ought not be credit given for "waiving constitutional rights."<sup>155</sup> Putting the questionable validity of his constitutional argument aside, the Senator fails to acknowledge that the practice of crediting defendants for waiving rights guaranteed under the Constitution is widely accepted throughout the criminal justice system.<sup>156</sup> For example, the Constitution guarantees all criminal defendants the right

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151. See Gabriel L. Imperato, *Internal Investigations, Government Investigations, Whistleblower Concerns*, 51 ALA. L. REV. 205, 226-30 (1999) (summarizing techniques employed by the government in corporate criminal investigations).

152. See discussion *supra* Parts II.A, C.

153. See *supra* text accompanying notes 126-31.

154. See Buell, *Criminal Procedure*, *supra* note 136, at 1660 ("[I]t is undeniably true that a firm's selection and funding of counsel for its agents, in relation to a situation where a firm does not do so, *does* impede [DOJ] regulation.").

155. *Comm. Hearing*, *supra* note 94, at \*10 (statement of Sen. Arlen Specter, Chairman, S. Comm. on the Judiciary).

156. As McNulty pointed out during his testimony at the Committee Hearing, "[T]housands of criminals today as we sit here will receive that very benefit for waiving a constitutional right." *Comm. Hearing*, *supra* note 94, at \*12.

to a jury trial.<sup>157</sup> Yet it is commonplace for criminal defendants to earn leniency in charging and sentencing decisions for waiving their constitutional right to trial and entering a plea.<sup>158</sup>

*D. The Executive Branch's Resolution is Inadequate*

The executive branch's response, via the McNulty Memo, attempts to address critics' concerns,<sup>159</sup> but the result is untenable. The Memo both places a general ban on the consideration of employee legal fees advancement, while at the same time admitting that legal fees advancement can, in some circumstances, be intended to impede investigations.<sup>160</sup> Indeed, it provides little guidance for prosecutors to identify the "extremely rare cases [when] advancement of attorney's fees may be taken into account."<sup>161</sup>

Moreover, the McNulty Memo's labeling of cases where payment of legal fees may be collusive conduct as "extremely rare"<sup>162</sup> is dangerously short-sighted. Especially in the corporate context, it is exceedingly difficult, if not impossible, to predict the frequency or manifestations that deceptive conduct of corporate insiders might assume.<sup>163</sup> Yet, the McNulty Memo's implication that collusion through the advancement of legal fees is unlikely to occur purports to do just that.<sup>164</sup> Even more troubling, by directing prosecutorial

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157. U.S. CONST. art. III, § 2, cl. 3.

158. See *Comm. Hearing*, *supra* note 94, at \*12 (testimony of Paul McNulty, Deputy Att'y Gen.). See also U.S. ATTY'YS' MANUAL *supra* note 17, § 9-27.400.B (setting out types of plea agreements whereby, in return for a defendant's plea to an offense, the prosecutor may dismiss other charges or request a reduced sentence); *U.S. Sentencing Commission Guidelines Manual* § 3E1.1(b) (2005) (allowing a reduction in sentence for entering a guilty plea).

159. See discussion *supra* Part II.D.

160. McNulty Memo, *supra* note 104, § VII.B.3.

161. *Id.* § VII.B.3 n.3. McNulty states that prosecutors should look at the "totality of the circumstances" but no further guidance is provided. *Id.*

162. *Id.*

163. Indeed, a primary contributing factor to the devastating effects of the Enron type financial crimes is that the "institutional watchdogs," including the DOJ, who work to protect investors from false or misleading information, were not able to see through the deceptive practices of corporate management. See Kroger, *supra* note 27, at 59–61. Kroger, a former prosecutor on the Enron Task Force, states that the "disaster occurred largely because of a troubling gap between [outsider] perception[s] and [company] reality." *Id.* at 59. Subsequent reforms have done little to combat this problem. *Id.* at 61.

164. Cf. McNulty Memo, *supra* note 104, § VII.B.3.

attention away from the possibility of collusion through the payment of employee legal fees, it opens the door for this practice to become more prevalent.

#### IV. PROPOSAL

The discourse presented in this Note has established a number of propositions. First, it is desirable for prosecutors to have the discretion to take a target corporation's cooperation into account when making their indictment decision.<sup>165</sup> Second, whether the corporation, while not legally obligated to do so, voluntarily pays the legal fees of wrongdoing employees is a relevant and important factor for prosecutors to take into consideration in weighing the value of the corporation's cooperation.<sup>166</sup> In that vein, any policy that purports to flatly ban prosecutors from considering a corporation's payment of legal fees to its culpable agents is ill conceived.<sup>167</sup> Finally, without a clearly defined standard to determine when the consideration of legal fees payment is legitimate, there is the possibility that prosecutors could either abuse their power, or at least cause corporations to "play it safe" and refuse to pay the legal fees of innocent employees.<sup>168</sup> Thus, any adequate solution must allow prosecutors the discretion to take into consideration legal fee advancement to culpable employees, and it must also set out a clear standard to inform prosecutors when employees are sufficiently culpable so as to make legal fee advancement an appropriate consideration under the circumstances.

To accomplish this, I propose a guideline which encourages prosecutors to credit a target corporation with leniency if it has cooperated with the government investigation. If, however, the corporation chooses to advance legal fees to its employees who are culpably involved in the underlying criminal misconduct, without a legal obligation to do so, it may be within the prosecutor's discretion to consider such behavior as uncooperative. Significantly, before a prosecutor may exercise that discretion, he or she must seek a judicial

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165. See discussion *supra* Part III.A.2.

166. See discussion *supra* Part III.A.3.

167. See discussion *supra* Part III.C.

168. See *supra* note 51 and text accompanying note 85.

determination, based on a showing of probable cause, that the employee is culpably involved in the underlying offense. Consistent with longstanding Supreme Court precedent, a showing of probable cause would require the prosecutor to proffer “enough particularized facts to lead a common sense person of reasonable caution to believe that there is a fair probability of criminal activity”<sup>169</sup> committed by the agent.

Like the apparent goal of the McNulty Memo,<sup>170</sup> this standard limits the discretion of prosecutors, so as to minimize, if not eliminate, the possibility of abuse. On the other hand, this standard differs from the McNulty Memo in several respects. First, it is significantly more practical for a prosecutor to simply seek a finding of probable cause from a local judge or magistrate rather than requiring every prosecutor in the country to seek approval from one person: the Deputy Attorney General.<sup>171</sup> Second, a judge is a neutral, and detached, party who can objectively review the request from a prosecutor.<sup>172</sup> The Deputy Attorney General, on the other hand, is a

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169. STEPHEN A. SALTZBURG ET AL., BOOK, CRIMINAL PROCEDURE 100 (3d ed. 2003) (citing *Illinois v. Gates*, 462 U.S. 213 (1983)). According to Supreme Court jurisprudence, “The rule of probable cause is a practical, nontechnical conception affording the best compromise that has been found for accommodating the [] often opposing interests” between safeguarding citizens’ rights and allowing law enforcement fair leeway to protect the community. *Brinegar v. United States*, 338 U.S. 160, 176 (1949). To that end, the degree of probability needed to establish probable cause is something “more than bare suspicion,” but “less than evidence which would justify condemnation.” *Id.* at 175–76.

170. *Cf.* McNulty Memo, *supra* note 104, at introductory cmt. (stating that the “adjust[ments] [to] certain aspects of” DOJ policy contained in the McNulty Memo are designed to “further promote public confidence in the Department”).

171. *Cf. id.* § VII.B.3 n.3 (“[A]pproval must be obtained from the Deputy Attorney General before prosecutors may consider” the advancement of attorneys’ fees).

172. One might argue that this standard would only add to the already heavy workload local judges and magistrates handle, thereby running the risk that judicial review of prosecutors’ evidence regarding employee culpability may be cursory at best. Craig D. Uchida & Timothy S. Bynum, *Search Warrants, Motions to Suppress and “Lost Cases:” The Effects of the Exclusionary Rule in Seven Jurisdictions*, 81 J. CRIM. L. & CRIMINOLOGY 1034, 1057–58 (1991) (finding that in at least one community, judges only spent an average of five to thirty minutes reviewing the evidence of probable cause for warrant applications, and that out of 1,748 warrant applications, only one was rejected). Whatever the risks, however, the Supreme Court has repeatedly held that a probable cause determination by “a neutral and detached judicial officer is a more reliable safeguard against [impingement on individual rights] than the hurried judgment of a law enforcement officer engaged in the often competitive enterprise of ferreting out crime.” *Lo-Ji Sales, Inc. v. New York*, 442 U.S. 319, 326 (1979) (examining probable cause in the setting of unreasonable searches). Moreover, a judicial officer is better

decidedly interested party.<sup>173</sup> Finally, and most important, the requirement of probable cause provides prosecutors with a clear standard, rather than the vague and contradictory guidance provided by the McNulty Memo.<sup>174</sup>

Additionally, this standard better comports with corporate interests. Under the McNulty Memo, a corporation still has no way to determine *ex ante* whether a prosecutor may seek approval to take the payment of legal fees into consideration. Therefore, given the stakes,<sup>175</sup> it is likely that a conservative corporation will still err on the side of caution and refuse payment of legal fees to its employees, whether culpable or not.<sup>176</sup> In contrast, under a probable cause standard, although there will still be some uncertainty, corporate counsel is provided with a much clearer projection of whether it risks adverse consequences from a decision to advance the legal fees of the corporation's employees under government investigation.

Moreover, a showing of probable cause will sufficiently address *Stein's* concern over the arguable property interests an individual may have flowing from an expectation to have his or her legal fees advanced.<sup>177</sup> Probable cause as a justification for impinging individuals' property rights under certain circumstances is a mainstay of constitutional jurisprudence. For example, in the context of the

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suited to maintain a standard of review that is at least as objective, if not more so, than the Deputy Attorney General, who may be prone to "rubber stamping" recommendations by local prosecutors or rejecting valid recommendations due to political pressures. *See infra* note 173 and accompanying text. Indeed, the promulgation of the McNulty Memo itself was at least partially in response to political pressure on the Deputy Attorney General. *See Comm. Hearing, supra* note 94, at \*11 (testimony of Paul McNulty, Deputy Att'y Gen.) ("Look, I've got [congressmen] upset. I've got former DOJ officials writing letters. We've got everybody complaining. The easiest thing for me to do today would be to . . . go ahead and change the [Thompson Memo] and make everybody happy.").

173. *See Coolidge v. New Hampshire*, 403 U.S. 443, 450 (1971) (The "chief government enforcement agent of the state—the Attorney General" is *per se* disqualified from determining sufficient probable cause to issue a warrant because "prosecutors and policemen simply cannot be asked to maintain the requisite neutrality with regard to their own investigations—the (competitive enterprise) that must rightly engage their single-minded attention.").

174. *See supra* notes 160–61 and accompanying text.

175. *See supra* note 112.

176. Indeed, this was a primary concern of many critics of the Thompson Memo. *See supra* note 51 and text accompanying note 85.

177. *See United States v. Stein*, 435 F. Supp. 2d 330, 367 (S.D.N.Y. 2006).

Fourth Amendment,<sup>178</sup> probable cause ordinarily justifies law enforcement's seizure (and search) of both person and property.<sup>179</sup> Even more analogous, the Supreme Court has held that, notwithstanding Fifth and Sixth Amendment guarantees,<sup>180</sup> in certain circumstances, probable cause justifies the government freezing a defendant's funds even "before he is convicted-and before [the funds] are finally adjudged to be forfeitable."<sup>181</sup>

### CONCLUSION

The Thompson Memo was fashioned as a quick and much-needed response to combat new developments in corporate crime and hold those responsible accountable.<sup>182</sup> Arguments that have been subsequently raised against its amorphous guidance regarding employee legal fees advancement have proven meritorious. The Thompson Memo's faults, however, are not adequately addressed by passing legislation or promulgating new guidelines that either restrict prosecutors from taking into account relevant and legitimate factors, or provide no further guidance on when those factors should be employed. In balancing the interests of innocent employees with legitimate law enforcement concerns, the proper solution is to provide a bright-line standard for determining when a target corporation's payment of legal fees is a legitimate consideration and how that determination must be made. Such a bright-line rule is attained by conditioning prosecutors' consideration of legal fee advancement on a judicial finding of probable cause that the employee is culpably involved in the underlying criminal offense of the corporation.

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178. U.S. CONST. AMEND. IV (protecting against unreasonable searches and seizures).

179. *See, e.g.*, *Whren v. United States*, 517 U.S. 806, 818 (1996) ("[T]he usual rule [is] that probable cause to believe the law has been broken 'outbalances' [the] private interest[s] in avoiding" impingement on Fourth Amendment rights.) (internal citations omitted).

180. U.S. CONST. AMEND. V, VI. The Sixth Amendment protects criminal defendants' right to choice of counsel and the Fifth Amendment "guarantees . . . a 'balance of forces' between the accused and the Government." *U.S. v. Monsanto*, 491 U.S. 600, 614 (1989).

181. *Monsanto*, 491 U.S. at 614–15. (holding that courts are authorized to enter a pre-trial order seizing a defendant's assets, even where those assets would be used to pay legal fees, if the assets would be subject to forfeiture upon conviction).

182. *See supra* Part I.B.