WHAT A GENERAL COUNSEL SHOULD KNOW ABOUT COMPLIANCE?

I. Teaser Questions:

What is compliance?

Is compliance a legal matter requiring client confidentiality?

Who is a compliance officer's client?

Does a compliance officer owe fiduciary or other duties to his employer?

Can a general counsel or his staff be "friends" with compliance staff?

II. Similarities and Differences

a. General Counsel -

i. Recent job descriptions for a general counsel position:

"The general counsel is responsible for leading corporate strategic and tactical legal initiatives. The general counsel provides senior management with effective advice on company strategies and their implementation, manages the legal function, represents the company in legal matters or obtains and oversees the work of outside counsel on behalf of the company. The general counsel is directly involved in complex business transactions by negotiating critical contracts."

"We are looking for an excellent General Counsel to add value to and be the "backbone" of our business. You will ensure that company operates within the law at all times, offer counsel on legal issues, create an effective guardian of the organization and facilitate business strategies development. The successful candidate will be able to ensure legal compliance and limit risk exposure."

ii. Key Components for General Counsel –

1. Knowledgeable advice to client
2. Representation of client
3. Protection of client
4. Candor with client

iii. Consistent with delegated duties

1. Board of Directors are responsible
    a. Del. Code Ann. title 8, § 141 (a) ("The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors…")
    b. K.S.A. 17-6301 (a) is similar
2. Whether private or governmental, certain duties / responsibilities are imposed upon controlling entity who, in turn, can delegate responsibility to subordinates
    a. Directors and Officers
        i. Board of Directors have fiduciary duty of care, loyalty, good faith – *Smith v. Van Gorkom*, 488 A.2d 858, 872 ((Del. S.Ct. 1985)

> "In carrying out their managerial roles, directors are charged with an unyielding fiduciary duty to the corporation and its shareholders. *Loft, Inc. v. Guth,* Del.Ch., 2 A.2d 225 (1938), *aff'd,* Del.Supr., 5 A.2d 503 (1939). The business judgment rule exists to protect and promote the full and free exercise of the managerial power granted to Delaware directors. *Zapata Corp. v. Maldonado, supra* at 782. The rule itself "is a presumption that in making a business decision, the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company." *Aronson, supra* at 812."

ii. Officers have fiduciary duties as well – Johnson & Garvis, "Are Corporate Officers Advised About Fiduciary Duties?", 64 Bus. Law 1105 (2008-2009); see, also, *Gantler v. Stephens*, 965 A.2d 695 (Del. 2009) for duty of loyalty

b. Governmental chiefs have fiduciary responsibilities
   i. Hobbs, "Personal Liability of Directors of Federal Government Corporations", Vol. 30, Issue 4, Case Western Reserve Law Review (1980).
   ii. Criddle, "Fiduciary Foundations of Administrative Law", 54 UCLA Law Review 117, (2006)

3. General Counsel operate under delegation of authority and share the fiduciary duties delegated by Board – Deborah A. Mott, "The Discrete Roles of General Counsel", 74 Fordham Law Review 955, (2005)

iv. Consistent with ethical canons tied to licensure -

1. "A lawyer is a representative of clients, an officer of the legal system and a public citizen having special responsibility for the quality of justice." KS. S. Ct. R. 226, "Preamble: A Lawyer's Responsibilities"
2. ABA STANDARDS FOR IMPOSING LAWYER SANCTIONS AS APPROVED, FEBRUARY 1986 AND AS AMENDED, FEBRUARY 1992, Copyright © 1992, by the American Bar Association –
   a. Duty of loyalty to client
   b. Duty of diligence to client
   c. Duty of competence to client
   d. Duty of candor to client

b. Compliance Officer –
   i. Recent job descriptions for a compliance officer position:

"Compliance officers must have a strong working knowledge of federal and state regulatory guidelines and standards. Monitoring accounting and regulatory guidelines as they relate to financial reporting and documentation also is important and requires excellent analytical, project management, communication and organizational skills. Compliance officers should possess knowledge of compliance standards and policies, audit techniques, regulatory issues, operations and procedures as they relate to the organization. Candidates should have a minimum of three to five years of experience in regulatory compliance. A bachelor's degree in accounting, business, finance or a related field is required, and a master's degree in business administration (MBA) or certification such as certified public accountant (CPA) is preferred."

"We are looking for a Compliance Officer to ensure that our operations and business transactions follow all relevant legal and internal rules. You will also review employees' work and provide advice on compliance. To succeed in this role, you should be a reliable professional who is not afraid to speak their mind and stand by their decisions. You should be familiar with risk management and our industry's standards. Your goal will be to ensure we operate in a legal and ethical manner while meeting our business objectives. If you also have a sharp business acumen, we'd like to meet you."

ii. Key Components –
    1. Knowledgeable advice to client
    2. Protection of client
    3. Candor with client

iii. "Duties" owed by compliance officer – similar analysis to General Counsel

c. Differences
    i. Representation of Client
    ii. Confidentiality
        1. Attorney Client Privilege

a. 5 C's – **c**onfidential **c**ommunication by **c**ounsel **c**ounseling **c**lient
b. K.S.A. 60-426 (a) - "(a) General rule. Subject to K.S.A. 60-437, and except as otherwise provided by subsection (b) of this section **communications** found by the judge to have been **between lawyer and his or her client** in the course of that **relationship** and **in professional confidence**, are privileged…" Emphasis added.

2. Confidentiality due to ethical canons –
   a. ABA Model Rules of Professional Conduct – Rule 1.6 (a) – "A lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent, the disclosure is impliedly authorized in order to carry out the representation or the disclosure is permitted by paragraph (b).")
   b. Kansas – similar – KRPC 1.6

III. First Question: Should the Legal Function be Separate from the Compliance Function?

a. Are the knowledge bases for each professional different?
   i. Yes and No
   ii. Both should have knowledge of their subject area
   iii. Both should be able to parse substantive and complex language
   iv. My opinion only – the attorney should handle representation

b. Does an attorney have the same focus as a compliance officer?

Ostlund, "Should We Separate the General Counsel & the Chief Compliance Officer?", Seton Hall Law School Student Scholarship 889 (2017) Link: https://scholarship.shu.edu/cgi/viewcontent.cgi?referer=https://www.google.com/&httpsredir=1&article=1897&context=student_scholarship (last accessed Sept. 1, 2019)

"The GC is the organization's highest ranking legal counselor. The GC's assists an organization to become more efficient and compliant, however, such involvement must not compromise the ability of the GC to "vigorously defend the organization after potential violations of the law have been identified." (citing to Hill, Peters, & Sawyer, "The Relationship between Compliance Officer, In-House Counsel, and Outside Counsel: An Essential Partnership for Managing and Mitigating Regulatory Risk", Am. Health Lawyers Ass'n. Fraud and Compliance Forum 4 (Oct. 6-7, 2014)

"At its most elemental, the CCO is responsible for developing the policies to ensure ethical and legally compliant behavior within a company, as well as procedures to detect, mitigate, and sanction ethical or legal malfeasance after it has occurred."

"Understanding the different mentality of the two roles may be helpful to illustrate how the GC and CCO are distinct. One commentator noted that a corporate lawyer is trained and employed to craft the law to best serve his or her client. It is natural, therefore, for such a lawyer to resist cooperation with government, except perhaps if doing so will help him or her to mitigate a client's penalty. Underlying compliance, is the obligation to report credible evidence of misconduct to the appropriate regulating agency. Therefore, while the CCO and the GC are similar, the CCO is focused on compliance detection, and resolution, whereas the GC's "duty is to protect [an organization's] liability profile." "

c. Litigation Differences – Implications of *North American Mortgage Investors v. First Wisconsin Nat'l Bank of Milwaukee*, 69 F.R.D. 9, 11 (E.D. Wis. 1975) *Georgia-Pacific Corp. v. GAF Roofing Manufacturing Corp.* 1996 WL 29392*3-*4 (S.D.N.Y. Jan. 25,1996), *Rusnak v. Dollar General Corp.*, 2005 WL 284074 *1(S.D. Ohio 2005) ("A lawyer, who functions as an investigator, is not functioning as a lawyer and not entitled to assert the [attorney-client] privilege.") and similar cases.

d. Crime / Fraud exception to attorney-client privilege when client attempts to use lawyer to commit or cover-up crime – Michmerhuizen, "Confidentiality, Privilege: A Basic Value in Two Different Applications", Ctr. For Prof'l. Responsibility.

IV. Second Question: If Legal and Compliance functions are to be combined, does the organization's structure / operations lend itself to manageable legal and compliance issues?

a. Can you wear too many hats? Kewalramani (Moses & Singer), "Confidentiality and Whistleblowing: Where In-House Counsel's Competing Interests Collide" Lexis Practice Advisor Journal (posted 6/22/2018). Accessed at: https://www.lexisnexis.com/lexis-practice-advisor/the-journal/b/lpa/posts/confidentiality-and-whistleblowing-where-in-house-counsel-s-competing-interests-collide . Last accessed on Sept. 2, 2019.

"While playing these roles, in-house counsel are mandated to act ethically under the rules of professional conduct, ensure that the corporate employer complies with applicable laws and regulations, and follow the direction of company management on corporate policies and practices. This rather complex assortment of functions can occasionally lead to conflicting–and often competing–loyalties. Are in-house counsel to act as officers of the court, upholding principles of professionalism and ethics while enforcing compliance with applicable laws, or are they to blindly protect the confidences and further the interests and objectives of their corporate employers without regard for legal and ethical compliance? These issues can give rise to unique ethical, moral, economic, and business dilemmas. This is because in-house counsel are ordinarily exposed to sensitive internal matters that could increase the potential for situations where it may be appropriate to blow the whistle on clients. Suppose an in-house counsel detects corporate wrongdoing. Would reporting such conduct violate the ethical duty of confidentiality and loyalty owed to the client and breach the attorney-client privilege? Or would the failure to disclose and report such unlawful activity constitute a violation of law and related ethics rules on reporting company wrongdoing? Can a fine balance be struck?"

b. Securities – Dartley, "The Combined Role of General Counsel and the Chief Compliance Officer – Opportunities and Challenges", Practical Compliance & Risk Management for the Securities Industry (May-June 2014)

"Furthermore, what happens if senior management is willing to take an aggressive position on whether the information constitutes material non-public information, and is willing to take on a higher regulatory risk in order to achieve the firm's investment management goals? In-house counsel's role in this circumstance is to advise senior management as to the degree of risk and the arguments that may be advanced if the matter is eventually questioned in the firm's next regulatory exam. The CCO's role, on the other hand, is to make a determination as to whether an aggressive position may be taken consistent with the firm's compliance program and the regulatory rules, and also whether the firm should take on this additional regulatory risk. One can see in this example the conflict that this dual role can produce. Recent commentary from the SEC on the Commission's expectations for chief compliance officers exacerbates the potential conflicts that can arise for individuals who serve as both in-house counsel and chief compliance officer. The SEC has made it clear that it expects chief compliance officers, and attorneys as well, to play a gatekeeping function."

c. Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204
    i. History – Perceived role of lawyers, accountants, officers, directors in Enron, WorldCom, Adelphia, Global Crossing financial debacles.
    ii. ABA spin on SOA - lawyers were perceived as contributing to the controversies.
    iii. Section 307, SOA, directed SEC to promulgate minimum standards of professional conduct for lawyers practicing before the SEC.
    iv. Standards included requirement that attorneys report evidence of material violation of securities law and permit disclosure of confidential information in certain scenarios.
    v. Outside Counsel is desirable since SOA applies to attorneys who practice before the SEC and who are in attorney-client relationship with affected entity - Koniak, Cohen, & Cramton,

"Legal and Ethical Duties of Lawyers after Sarbanes-Oxley", Boston University School of Law Working Paper No. 04-20. All 96 pages available at: http://www.bu.edu/law/workingpapers-archive/documents/koniak-et-al-sarbanes-oxley-04-20.pdf (last accessed on Sept. 1, 2019)

"Lawyers who are not securities lawyers would have a good argument that, at least with respect to evidence outside their area of expertise, reporting evidence of a material violation to the securities lawyer who is handling the SEC filing would be sufficient because the securities lawyer would be acting in a supervisory capacity. Second, as a practical matter, the sanctions the SEC can impose on non-securities lawyers are limited. The SEC can, for example, preclude the lawyer from appearing and practicing before the SEC for a period of time, but if that simply means the lawyer cannot give an opinion about material to be included in an SEC filing, that may not put a large dent in the non-securities' lawyer's (and more importantly, his firm's) practice"

"It is not clear that the exemption in §205.2(a)(2)(i) was necessary at all. In the first place, the duty to report under §205.3(b) is limited to an attorney "appearing and practicing before the Commission in the representation of an issuer." "In the representation of an issuer" is defined in§205.2(g) to mean "providing legal services as an attorney for the issuer, regardless of whether the attorney is employed or retained by the issuer." That definition seems to resolve the problem of lawyers who are employed by issuers but do not practice law. Even without that limiting definition, most of the conduct listed in "appearing and practicing" involves the practice of law, rather than "mere business" activity."

d. Corporate Crime – Memorandum from Sally Quillan Yates, U.S. Dep't. of Justice, "Individual Accountability for Corporate Wrongdoing" (Sept. 9, 2015). Accessible at

https://www.justice.gov/archives/dag/file/769036/download (last accessed Sept. 1, 2019)

"In order for a company to receive any consideration for cooperation under the Principles of Federal Prosecution of Business Organizations, the company must completely disclose to the Department all relevant facts about individual misconduct. Companies cannot pick and choose what facts to disclose. That is, to be eligible for any credit for cooperation, the company must identify all individuals involved in or responsible for the misconduct at issue, regardless of their position, status or seniority, and provide to the Department all facts relating to that misconduct. If a company seeking cooperation credit declines to learn of such facts or to provide the Department with complete factual information about individual wrongdoers, its cooperation will not be considered a mitigating factor pursuant to USAM 9-28.700 el seq."

Practice: DOJ uses deferred prosecution agreements (DPAs) to obtain corporate cooperation and get offending organizations to change their behavior to help mitigate future misconduct. A corporate ethics and compliance program and independent compliance auditing requirement are fairly standard parts of a DPA.

e. HHS OIG Corporate Integrity Agreements
    i. Corporate Integrity Agreements (CIA's) used in civil false claims to avoid federal health care exclusions – see "Corporate Integrity Agreements" at https://oig.hhs.gov/compliance/corporate-integrity-agreements/index.asp

    ii. "A comprehensive CIA typically lasts 5 years and includes requirements to:

- hire a compliance officer/appoint a compliance committee;
- develop written standards and policies;
- implement a comprehensive employee training program;
- retain an independent review organization to conduct annual reviews;
- establish a confidential disclosure program;
- restrict employment of ineligible persons;

- report overpayments, reportable events, and ongoing investigations/legal proceedings; and
- provide an implementation report and annual reports to OIG on the status of the entity's compliance activities."

Practice Question: Does signing a CIA provide a basis for a governmental health care program to trigger "credible allegations of fraud" review under 42 C.F.R. 455.23 ?

f. Hybrid Entities – Kansas Department of Health & Environment
   i. KDHE is a self-reported hybrid entity
   ii. KDHE has 3 divisions – Environment, Public Health, & Health Care Finance
      1. HCF is a covered entity due to Medicaid and State Employee Health programs
      2. Public Health is hybrid since some of its Bureaus use PHI (Bureau of Disease Control & Prevention) while others do not (Bureau of Health Promotion)
      3. Environment does not handle PHI
   iii. Kansas Medicaid and some of the Public Health programs share PHI – school-age children via IDEA, immunizations, farm workers
   iv. Due to hybrid status, CMS treats each KDHE division as its own entity and required intra-agency agreements between the divisions.
   v. Can one compliance officer handle all parts?

V. Third Question: Should a GC promote a robust compliance program as a legal defense strategy?

a. Rhetorical Answer – **YES**

b. *In re Caremark Int'l., Inc. Derivative Litigation*, 698 A.2d 959 (Del. Ch. 1996)
   i. Caremark International provided health care services and products to patients referred to them by physicians. It had approximately 7,000 employees spread over 90 de-centralized branch operations.

ii. Caremark entered into financial arrangements with physicians prior to 1991 that paid certain fees to physicians who handled Medicare / Medicaid patients.
iii. Most of these arrangements set up / managed by junior officers of Caremark.
iv. Board of Directors were, generally, clueless.
v. In 1991, HHS issued clarifying regulations on "safe harbor" financial relationships in referral situations (see 42 C.F.R. 411.355 (b)) which triggered Board attention
vi. In the 1991 – 1994 period, Caremark took steps to assure compliance with federal Anti-Referral Payments Law (ARPL – precursor to Anti-Kickback provisions) including internal and external compliance / ethics audits with disclosure to Board. Board directed new policies and increased management supervision.
vii. In 1994, US DOJ, at HHS urging, sought civil remedies and criminal indictments (around $250 million) against Caremark for violation of the federal Anti-Referral Payments law for the past activity.
viii. Subsequently, 5 shareholders sought a derivative action due to "failure of the Board to act" despite fiduciary duties to exercise care and oversight.
ix. Compliance advice saves the Board

"1. Knowing violation for statute: Concerning the possibility that the Caremark directors knew of violations of law, none of the documents submitted for review, nor any of the deposition transcripts appear to provide evidence of it. Certainly, the Board understood that the company had entered into a variety of contracts with physicians, researchers, and health care providers and it was understood that some of these contracts were with persons who had prescribed treatments that Caremark participated in providing. **The board was informed that the company's reimbursement for patient care was frequently from government funded sources and that such services were subject to the ARPL. But the Board appears to have been informed by experts that the company's practices, while contestable, were lawful. There is no evidence that reliance on such reports was not reasonable. Thus, this case presents no occasion to apply a principle to the effect that knowingly**

causing the corporation to violate a criminal statute constitutes a breach of a director's fiduciary duty."

"2. Failure to monitor: Since it does appear that the Board was to some extent unaware of the activities that led to liability, I turn to a consideration of the other potential avenue to director liability that the pleadings take: director inattention or "negligence". Generally where a claim of directorial liability for corporate loss is predicated upon ignorance of liability creating activities within the corporation, as in Graham or in this case, **in my opinion only a sustained or systematic failure of the board to exercise oversight such as an utter failure to attempt to assure a reasonable information and reporting system exits will establish the lack of good faith that is a necessary condition to liability**…**Here the record supplies essentially no evidence that the director defendants were guilty of a sustained failure to exercise their oversight function.** To the contrary, insofar as I am able to tell on this record, the corporation's information systems appear to have represented a good faith attempt to be informed of relevant facts. If the directors did not know the specifics of the activities *972 that lead to the indictments, they cannot be faulted."

c. *Caremark* was precursor of increasing compliance requirements for activities involving governmental oversight and Directors knowledge concerning those compliance activities – Langevoort, "*Caremark* and Compliance: A Twenty Year Lookback", 90 Temple L. Rev. 727-742 (2018).

"But we need not obsess over history. *Caremark* is at the very least a label attached to what all now agree is a necessary and proper subject of attention for every board of directors: corporate compliance as a function within the broader task of enterprise risk management."

Today, however, I doubt that well-advised boards take this position (though some probably wish they could). The reason, once again, stems mainly from pressures from regulators and enforcers at the federal level who have come to believe in the value of a stronger board-level presence in compliance. The Organizational Sentencing Guidelines, Committee of Sponsoring Organizations of the Treadway

Commission principles, and numerous regulatory pronouncements seek not only board approval of written policies and procedures and key compliance personnel decisions, but also a much more interactive involvement that includes reporting lines running from the chief compliance officer (and perhaps chief legal officer) directly to the board, unfiltered by senior executives."

VI. Specific Compliance Areas that Require Competence by both a GC and a CCO whether combined or separated

a. HIPAA / Privacy Act
b. Reporting
c. Licensure
d. Financial
e. Records Retention
f. Social Media

VII. Epilogue – "Authorized Representative"

a. Person on Medicaid for a number of years.
b. Person had a DPOA for healthcare decisions and representative payee for Social Security
c. Person dies leaving a home valued at $60,000
d. State has an estate recovery claim for $100,000 for 5 years of Medicaid payments
e. State starts an estate proceeding as a creditor and seeks to sell the home to recover against the previously paid Medicaid payments.
f. The state's probate claim includes an itemization of paid medical reimbursements.
g. A hospital, who has an unpaid medical bill for services provided to the decedent from 3 years back, asks the state for the decedent's Medicaid records.
h. Do you provide the records?