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DOJ Guidance Offers Needed Flexibility For Corporate Fines

By **Ephraim (Fry) Wernick and Brittany Harwood** (October 29, 2019, 3:23 PM EDT)

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A new U.S. Department of Justice policy provides for additional transparency and long-needed guidance to prosecutors who often evaluate inability-to-pay claims by companies facing substantial criminal fines and penalties. In a potentially significant move, the DOJ's new policy also presents new opportunities for companies to advocate for reduced penalties with arguments that have not been available of late.

Over the past several years, a company seeking a reduced fine or penalty due to an inability to pay was forced to make the case that its continued viability would be substantially jeopardized were it to pay a fine that was called for under Chapter 8 of the U.S. Sentencing Guidelines. The DOJ's new policy memo, however, includes an important footnote that authorizes federal prosecutors to consider reducing criminal penalties to the extent needed to avoid severe collateral consequences.

This welcome change allows for increased flexibility and should open the door to more thoughtful negotiations between companies and prosecutors as they search to achieve the goals of punishing and deterring misconduct while also avoiding unnecessary harm to innocent shareholders, employees and third parties.

The DOJ's Continued Focus on Transparency

On Oct. 8, Assistant Attorney General Brian Benczkowski of the DOJ's Criminal Division announced a new policy[1] to help prosecutors evaluate a company's claim that it is unable to pay a criminal fine or penalty. Following through on earlier statements that were made by Deputy Assistant Attorney General Matthew Miner in September, Benczkowski announced the DOJ's release of a new policy memo and accompanying questionnaire to provide guidance and a framework for federal prosecutors to follow.

By making the DOJ's internal policy memo public, the DOJ continued a recent pattern aimed at increasing transparency and visibility for the business community to better understand the government's expectations and practices in corporate cases. For example, the DOJ adopted and publicized its Foreign Corrupt Practices Act Corporate Enforcement Policy, or CEP, in November 2017, which set forth explicit expectations and rewards for companies that self-report and/or cooperate with the government.

More recently, the DOJ's civil fraud director announced significant policy developments in False Claims Act cases and Miner twice made announcements over the past 16 months signaling the DOJ's focus on rewarding companies who self-report corruption that was uncovered after a corporate merger or acquisition.

In his remarks, Benczkowski discussed the Criminal Division's focus on enforcement and crime prevention.[2]

He explained that the DOJ was promoting transparency because it is helpful both internally and externally. Internally, these policies and guidelines ensure consistency and predictability in how standards are applied; externally, this allows the process to be more efficient and productive because the defense bar and business community are aware of the standards and expectations of prosecutors who make key decisions.[3]

Benczkowski added that the department wanted companies to "have the information and security they need to invest fully in compliance on the front end, and to make good decisions in the face of misconduct on the back end."[4]

The Inability-to-Pay Memo and Framework for Evaluating Claims

The department's new policy is set forth in Benczkowski's memo, entitled "Evaluating a Business Organization's Inability to Pay a Criminal Fine or Criminal Monetary Penalty." The memo lays out a multistep process prosecutors should follow in evaluating and addressing any inability-to-pay claims.

As a preliminary matter, a company must first agree with the DOJ concerning its desire to resolve its criminal exposure, including an agreement as to the form of the corporate criminal resolution — e.g., whether the company will plead guilty, enter into a deferred prosecution agreement, or DPA, or a agree to a nonprosecution agreement, or NPA — and the corresponding criminal fine or penalty.[5]

Once the agreed-upon criminal fine and penalty are determined, the company then may assert its claim that is unable to pay the applicable amount. Under the policy, the "burden of establishing the inability to pay rests with the business organization making such a claim."[6]

Attached to the DOJ's policy memo was an inability-to-pay questionnaire, which each company now will be required to complete and submit when making an inability-to-pay claim. This questionnaire prompts the company to provide specific information to the DOJ and requests documentation that will be required to enable prosecutors to evaluate the claim.

The questionnaire includes requests for the following:

- All cash flow projections and supporting documentation for the past year;
- All operating budgets and projections of future profitability created in the past year;
- All capital budgets and projections of annual capital expenditures created in the past year;
- Proposed changes in financing or capital structure;
- Acquisition or diversion plans;

- Restructuring plans;
- Claims to insurers;
- Related or affiliated party transactions;
- Encumbered assets;
- Liens on the company's assets; and
- Additional materials, if necessary — e.g., complete financial statements and tax returns dating back five years, appraisal and valuation materials, accounts receivable and accounts payable reports, credit agreements, top employees' compensation plans, and reports to lenders.[7]

The memo recognizes that there will be times when "legitimate questions exist regarding an organization's inability to pay, the analysis can be more complex."[8] Under such circumstances, prosecutors are instructed that they may also consider the following factors:

- Background on the company's financial condition (assessing the cause of the company's financial condition and whether capital extractions or related-party transactions have caused the lack of liquidity);
- Alternative sources of capital (assessing whether the company can raise additional capital through lines of credit or sales of equity or assets);
- Collateral consequences (assessing any potential significant adverse collateral consequences that may result from the imposition of a criminal fine or penalty such as inability to fund pension obligations, cause layoffs, or significantly disrupt the market);[9] and
- Victim restitution considerations (considering whether the criminal fine or penalty will impair the company's ability to provide restitution to victims).

After evaluating the relevant factors and considerations, if a prosecutor determines that a company is unable to pay the agreed-upon fine, then the government should recommend "an adjustment to the monetary penalty amount, but only to the extent necessary to avoid (1) threatening the continued viability of the organization and/or (2) impairing the organization's ability to make restitution to victims."[10]

The Importance of Footnote 4

While the new policy is helpful insofar as it sets forth a more uniform approach to evaluating inability-to-pay claims, perhaps the most important feature of the memo for the business community is contained in a footnote. In relevant part, Footnote 4 of the memo reads:

> Criminal Division attorneys may, where appropriate, make an adjustment to a proposed criminal fine or monetary penalty based on the existence of a significant adverse collateral consequence that, while severe, may not necessarily threaten the continued viability of the organization. In such cases, the adjustment to the monetary penalty amount should not be more than necessary to avoid causing the severe adverse collateral consequence at issue.[11]

This language affords far more flexibility to prosecutors and is a marked departure from how they have approached inability-to-pay claims in recent history. For example, in 2018, the DOJ entered into a DPA with Transport Logistics International Inc., a Maryland-based logistics company that admitted to bribing a Russian official to obtain lucrative contracts to ship nuclear fuel between Russia and the United States.

As part of the DPA, the DOJ accepted the company's inability-to-pay argument and reduced the criminal fine from $21 million to $2 million, because "a penalty greater than $2 million would substantially jeopardize the continued viability of the Company."[12]

Similarly, in 2017, SBM Offshore N.V., a Dutch oil and gas company, entered into a DPA with the DOJ and admitted to bribing officials in Brazil, Angola, Equatorial Guinea, Kazakhstan and Iraq.[13] The department accepted SBM's inability-to-pay argument and agreed to reduce its criminal fine to $238 million down from a range of $4.5 billion to $9 billion, at least in part to "[avoid] … a penalty that would substantially jeopardize the continued viability of the Company."[14]

The DOJ's Antitrust Division seems to have followed the same approach as the Criminal Division. In 2017, the DOJ entered into a plea agreement with Bumble Bee Foods LLC, in which the company admitted to price fixing in violation of the Sherman Act.

In the DOJ's sentencing memo, the department explained that it had engaged an outside accounting firm, and after assessing Bumble Bee's historic performance, current financial position and strength of its balance sheet, and future forecasts for the company and the packaged-seafood industry as a whole, the DOJ determined that Bumble Bee could not pay a "guidelines range fine."[15]

As a result, the department agreed to a reduced fine from $136.2 million to $25 million, because the lower amount was something that "Bumble Bee can pay without substantially jeopardizing its continued viability."[16]

Although the DOJ's guidance to prosecutors in Footnote 4 of the inability-to-pay memo seems to be a departure from recent practice,[17] the more nuanced approach is not entirely without precedent.

For example, in 2014, the DOJ entered into a plea agreement with Alcoa World Alumina LLC, which admitted to bribing government officials in Bahrain. The DOJ accepted the company's inability-to-pay argument and reduced the fine from at least $446 million to $209 million because of the "potential to substantially jeopardize Alcoa's ability to compete."[18]

In Alcoa, the DOJ found the company's inability-to-pay claim persuasive specifically because the company would not be able to "fund its sustaining and improving capital expenditures, its ability to invest in research and development, its ability to fund its pension obligations, and its ability to maintain necessary cash reserves to fund its operations and meet its liabilities."[19] the DOJ also allowed the company the opportunity to pay its penalty on an installment plan due to the "undue burden" that immediate payment would have had on the company.[20]

What This Means for You

Given the above, it seems that the DOJ's new policy guidance, and particularly Footnote 4 of the inability-to-pay memo, may forecast a significant policy change in how prosecutors will view inability-to-pay claims moving forward. There now is the ability to move away from the "substantially jeopardizing" the "continued viability" standard that was required in the past to a far more reasonable severity standard.

The new policy should invite new arguments and allow for more nuanced negotiations when a company seeks to lower its fine or penalty based on the harshness of collateral consequences, even if a guidelines-range penalty otherwise would fall short of bankrupting the company.

Among other things, companies now may be in the position to argue that a severe fine could trigger massive layoffs, hurt market competitiveness or cause a large drop in the value of a company, which could hurt innocent employees, investors and consumers, and also negatively impact the ability to compensate victims.

The current guidance instructs prosecutors to entertain such arguments when legitimate questions exist about a company's ability to pay. Companies should be encouraged by the DOJ's move toward transparency and better engagement with the business community.

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Disclosure: Wernick previously served as assistant chief of the FCPA Unit within the Department of Justice, Criminal Division, Fraud Section. He prosecuted the above-referenced case against Transport Logistics International, which included a fine reduction based on the company's inability to pay. This article and the reference to the TLI case rely solely on the publicly available information.

[1] Brian A. Benczkowski, Assistant Attorney General, U.S. Dep't of Justice, "Evaluating a Business Organization's Inability to Pay a Criminal Fine or Criminal Monetary Penalty" (Oct. 8, 2019), https://www.justice.gov/opa/speech/file/1207576/download.

[2] Brian A. Benczkowski, Assistant Attorney general, U.S. Dep't of Justice, Remarks as Prepared for Delivery, Global Investigations Review (Oct. 8, 2019) ("Benczkowski Speech"), https://www.justice.gov/opa/speech/assistant-attorney-general-brian-benczkowski-delivers-remarks-global-investigations.

[3] Id.

[4] Id.

[5] In determining the criminal penalty, prosecutors should consult: (1) the statutory sentencing factors in 18 U.S.C. § 3572(a) & (b); (2) guidance set forth in U.S.S.G. §§ 8C2.2 & 8C3.3; and (3) the Justice Manual regarding the consideration of collateral consequences in resolving a criminal case against a business organization. The memo also stated that prosecutors generally will need to consult an accounting expert to "examine the financial condition of the business." Inability-to-pay memo at 1.

[6] Id. at 2.

[7] Id. at 5.

[8] Id. at 3.

[9] While such collateral consequences should be considered by prosecutors in making their assessment, the memo cautions against considering other types of collateral consequences, such as how a criminal fine could impact future growth, planned or future product lines, future dividends, or planned hiring or retention. Id.

[10] Id. at 4.

[11] Id. at n4 (emphasis added).

[12] Deferred Prosecution Agreement, United States v. Transport Logistics International Inc., No. 8:18-cr-00001 (TDC), at 5 (D. Md. Mar. 12, 2018) (emphasis added).

[13] Deferred Prosecution Agreement, United States v. SBM Offshore N.V., No. 17-cr-686 (S.D.T.X. Nov. 29, 2017).

[14] Id. at 7, 13 (emphasis added).

[15] Sentencing Memorandum, United States v. Bumble Bee Foods LLC, No. 3-17-cr-00249 (EMC), at 13-14 (N.D. Cal. Jul. 31, 2017).

[16] Id. at 10, 14 (emphasis added).

[17] Not every recent inability-to-pay case has included the "substantial jeopardy" to "continued viability" language. In the FCPA case against Odebrecht S.A., a Brazilian construction firm that admitted to bribing foreign officials at Petrobras, the DOJ was notably silent as to the standard they adopted when agreeing to accept the inability-to-pay claim. The DOJ ultimately agreed to reduce the total criminal fine and penalty that Odebrecht would receive from $4.5 billion to $2.6 billion, and DOJ agreed to accept an installment payment plan for the company to pay the DOJ, Swiss and Brazilian authorities. After entering into the DPA, the DOJ later agreed to reduce its take of the total fine from $117 million to only $93 million as a result of Odebrecht's deteriorating financial condition. Sentencing Memorandum, United States v. Odebrecht S.A., No. 16-cr-643 (RJD) (E.D.N.Y. Apr. 11, 2017). Although the relevant filings fail to include explicit language stating that the reduction was due to the substantial threat to the continued viability of the company, it certainly seems as though that was the DOJ's standard. After all, on June 17 Odebrecht filed for bankruptcy after years of dealing with the fallout from the criminal probes and resolution.

[18] Plea Agreement, United States v. Alcoa World Alumina LLC, No. 14-cr-0007, at 15 (W.D. Pa. Jan. 8, 2014) (emphasis added).

[19] Id. at 15-16.

[20] Id. at 15.