In-house Counsel in the Crosshairs

At present, the government's appetite for fighting corporate fraud and malfeasance may be uncertain. Nonetheless, it is now well established that corporate counsel and compliance professionals are not immune from civil or criminal liability that might previously have been reserved for directors and business executives. The criminal trial of Evan Greebel, which began in October 2017, serves as a recent reminder that lawyers can and do become prosecution targets due to their work for a client. Greebel, a former law firm partner, served as corporate counsel for Retrophin Inc., founded by the now-imprisoned pharmaceutical executive Martin Shkreli.[1] Prosecutors accused both Shkreli and Greebel of conspiracy to commit wire and securities fraud involving the company. Pretrial proceedings reflect that Shkreli would raise an "advice of counsel" defense to try to show that he lacked fraudulent intent, while Greebel would contend that Shkreli lied and failed to disclose material information to him.[2] From an attorney's perspective, the case raises several interesting issues relating to an attorney's ethical obligations, fiduciary duties, and interest in avoiding personal liability.

Although Greebel worked as outside counsel, he could have found himself in the same situation as an in-house attorney. Indeed, in recent years, in-house counsel and compliance officers have been targeted in criminal and civil investigative or enforcement proceedings. This paper identifies some of the common scenarios in which they have become targets, by discussing examples of prosecution of in-house professionals. In addition to potential criminal or civil exposure, in-house counsel's decisions in these scenarios implicate the rules of professional responsibility to which attorneys are subject. Thus in identifying the types of attorney conduct that resulted in criminal or civil complaints, the paper also discusses the professional ethics rules that may be relevant to the examples. The paper ends with a discussion of the question, "What choices do in-house counsel have when their organizational clients have violated or are about to violate the law?"

In discussing the ethics rules, this paper refers to the American Bar Association's Model Rules of Professional Conduct. States vary in the specific formulations of the ethical rules adopted. Accordingly, any specific situation should be assessed with reference to the applicable state rules.

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[1] Christine Simmons, *Shkreli's Ex-Katten, Kaye Scholer Lawyer Faces Skeptical Judge Ahead of Trial*, NEW YORK LAW JOURNAL (Oct. 6, 2017), https://www.law.com/newyorklawjournal/almID/1202799897318; Christie Smythe, *Shkreli Lawyer, on Trial Himself, Seeks Distance From Shkreli*, BLOOMBERGTECHNOLOGY (Oct. 20, 2017, 2:23 PM), https://www.bloomberg.com/news/articles/2017-10-20/shkreli-lawyer-on-trial-himself-seeks-distance-from-shkreli.

[2] *United States v. Shkreli*, No. 15–CR–637(KAM), 2017 WL 4019387, at *1 (E.D.N.Y. Apr. 19, 2017).

1. Scenarios in which in-house counsel and compliance professionals become targets in governmental proceedings

A. Allegations of independent criminal activity

Perhaps the most unsurprising scenario in which an in-house practitioner becomes a target is when he or she independently engages in criminal activity, e.g. insider trading, without the knowledge or involvement of others at the company. This scenario implicates at least a couple of provisions of Model Rule 8.4. That rule identifies actions amounting to "professional misconduct."[3] The comment on the rule confirms that attorneys are subject to discipline when they violate the Rules of Professional Conduct.

Model Rule 8.4(b) and (c) generally would be implicated when an attorney engages in criminal activity in the work context. Rule 8.4(b) makes it professional misconduct to "commit a criminal act that reflects adversely on the lawyer's honesty, trustworthiness or fitness as a lawyer in other respects." The comment to the rule explains that not all crimes fit within the scope of the rule, because not all of them reflect adversely on a lawyer's fitness to practice law. Offenses involving fraud, violence, dishonesty, breach of trust, or serious interference with the administration of justice would be covered by the rule. But offenses traditionally characterized as involving "moral turpitude" would not. The comment does clarify that a "pattern of repeated offenses, even ones of minor significance when considered separately," can be problematic. [4] Model Rule 8.4(c) provides that even when the conduct does not amount to a crime, if it involves "dishonesty, fraud, deceit or misrepresentation," it would be professional misconduct.

A crime in this context also likely would implicate the ethical rules limiting an attorney's use of a client's confidential information. Model Rule 1.8(b) prohibits an attorney from using "information relating to representation of a client to the disadvantage of the client" in the absence of informed consent or an exception under the rules.[5] The comment to the rule explains that the prohibition applies when the client's information is used to benefit the lawyer or a third party. Model Rule 1.9(c) places an analogous restriction on a lawyer's use of information of a former client.

Examples:

Kevin Heron, Amkor Technology, Inc. – In 2007, the former general counsel of Amkor Technology, Inc., Kevin Heron, was convicted of conspiracy to commit securities fraud and securities fraud.[6] The government had brought insider trading charges against him in connection with a series of personal trades in Amkor stock while he possessed material, non-public information about Amkor's financial performance and business transactions. At the relevant time, Heron served as Amkor's chief insider trading compliance officer, in addition to being its

[3] Model Rules of Prof'l Conduct R. 8.4.

[4] Comment on Model Rules of Prof'l Conduct R. 8.4.

[5] Model Rules of Prof'l Conduct R. 1.8.

[6] *See U.S. v. Heron*, 323 Fed. Appx. 150 (3rd Cir. 2009).

general counsel. One of his illegal trades involved the purchase of 4000 shares of Amkor stock for approximately $60,000 two weeks before the company released a quarterly earnings report. He purchased the stock at a time when the company's own policy barred employees from trading Amkor stock. Soon after the earnings release, Heron sold 75% of those shares for a profit of $115,000.

After his conviction by a jury on four counts, the trial court granted Heron's motion for acquittal on three of them, finding insufficient evidence to support the convictions. Although the trial court denied acquittal on the fourth count, it refused a sentencing enhancement, pursuant to a Sentencing Guideline provision, for abuse of a position of trust. The government appealed the acquittal and sentencing decisions. In a 2009 opinion, the Third Circuit reversed the district court on both issues. It found sufficient evidence to support the jury's verdict. On the sentencing enhancement, the appellate court found that as the chief insider trading compliance officer convicted of insider trading, Heron "clearly fits" within the category of abusers of positions of trust envisioned by the Sentencing Guidelines.

In addition to the criminal conviction, Heron faced a civil complaint by the SEC.[7] He settled the matter in 2009, consenting to a permanent injunction barring him from serving as an officer or director. He also consented to an administrative order by the Commission suspending him from appearing or practicing before it. In 2010, the Pennsylvania Supreme Court approved Heron's consent disbarment.[8]

John Rogicki, Train Babcock Advisors LLC. – In October 2017, the SEC filed a civil complaint against John Rogicki, the managing director and chief compliance officer of Train Babcock Advisors, an investment advisory firm.[9] The SEC alleges that Rogicki stole approximately $11 million from a charitable foundation set up for a client. He served as president and trustee of the foundation as well as its investment advisor, through Train Babcock. He made all investment decisions for the foundation. He also controlled the purchase and sale of securities in its advisory account at Train Babcock. The complaint alleges that Rogicki carried out his fraud between 2004 and 2016 primarily by liquidating securities positions in the advisory account and transferring the proceeds to himself. The complaint charges him with violations of the Investment Advisers Act of 1940 and the Securities Exchange Act of 1934. The Manhattan district attorney filed criminal charges against him.

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[7] Litigation Release No. 20851, Securities and Exchange Commission (Jan. 13, 2009), *available at* https://www.sec.gov/litigation/litrereleases/2009/lr20851.htm.

[8] Andrew Hard, *This Boot's for you: Former Amkor Technology General Counsel Disbarred*, CORPORATECOUNSEL (Feb. 10, 2010), https://www.law.com/corpcounsel/almID/1202443007269/.

[9] Litigation Release No. 23970, Securities and Exchange Commission (Oct. 19, 2017), *available at* https://www.sec.gov/litigation/litreleases/2017/lr23970.htm.

B. Allegations of participation in criminal activity with business associates

A relatively typical scenario in which an in-house attorney or compliance professional might become a defendant is in a prosecution directed at an alleged conspiracy involving multiple players at a company. In addition to the ethics rules relevant to a crime by an attorney acting alone, this scenario implicates the rules relating to advice provided to clients. Model Rule 1.2(d) provides that a lawyer may "not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent."[10] The rule does, however, explicitly allow a lawyer to "discuss the legal consequences of any proposed course of conduct with a client and may counsel or assist a client to make a good faith effort to determine the validity, scope, meaning or application of the law."[11]

As the comments on Rule 1.2(d) indicate, navigating the bounds of permissible and impermissible lawyering may become tricky, especially once the client's course of action has begun or is ongoing. If the course of action has begun, an attorney must tread carefully with respect to actions that might be construed as assisting with a crime or fraud. If the misconduct has already ceased, care must be exercised to ensure that advice cannot be cast as part of a cover-up.

The scenario may also trigger an attorney's obligations under Model Rule 1.13. That rule confirms that when an organization employs an attorney, the organization (rather than executives or other employees) is the lawyer's client. Rule 1.13(b) requires a lawyer who knows that someone else in the organization intends to violate an obligation to the organization or violate a law "that reasonably might be imputed to the organization, and that is likely to result in substantial injury to the organization" to proceed in the best interest of the organization.[12] The Rule goes on to specify that unless the lawyer reasonably believes it unnecessary to the organization's best interests, the lawyer must "refer the matter to higher authority in the organization, including, if warranted by the circumstances to the highest authority that can act on behalf of the organization as determined by applicable law."[13] The comments to the rule indicate that ordinarily referral to a higher authority would be necessary. An exception might be where the employee innocently misunderstood the law, but can be convinced to avoid the violation by the lawyer. The comment also cautions that any measures taken should be done in a way that minimizes the "risk of revealing information relating to the representation to persons outside the organization."[14]

If the highest authority fails to act, Rule 1.13 allows a lawyer to take certain actions. Moreover under Model Rule 1.16, a lawyer must withdraw from representation of a client if the

[10] Model Rules of Prof'l Conduct R. 1.2(d).

[11] *Id.*

[12] *Id.* at R. 1.13(b).

[13] *Id.*

[14] Comment on Model Rules of Prof'l Conduct R. 1.13.

representation "will result in violation of the rules of professional conduct or other law."[15] These provisions are discussed further in Section 2 below.

Examples:

Timothy Muir, AMG Services – Timothy Moore was indicted in federal court along with Scott Tucker for running an unlawful enterprise that charged usurious debt in violation of various laws. Tucker owned and controlled various "payday lending" businesses that were operated through AMG Services.[16] Muir served as general counsel for AMG starting in 2006. The indictment alleged that between 1997 and 2013, the enterprise led by Tucker charged consumers interest rates as high as 700%, in violation of various laws that cap annual rates. After various state legal actions against the businesses, Tucker entered into business relationships with three Indian tribes. The indictment alleged that the relationships were shams intending to use tribal sovereign immunity as a shield against the usury laws. According to the indictment, Tucker arranged to have tribal members "press a key on a computer" every day to supposedly approve hundreds of thousands of loans on tribal land, all of which had already been approved elsewhere. Once he became involved, the indictment alleged that Muir architected the arrangements with tribes. Allegedly he joined Tucker in providing materially false and misleading affidavits to courts about the tribes' purported control of the businesses. According to the indictment, Tucker owned, led and controlled a criminal enterprise, with Muir also acting as a leader.

The defendants filed a motion to dismiss the indictment, which the court denied in early 2017. The indictment charged the defendants under various provisions of the Racketeer Influenced and Corrupt Organizations Act directed at the collection of "unlawful debts." The defendants argued that the debts could not be "unlawful" because the rates were set by Indian tribes, whose sovereign authority allowed them to charge the rates, unless expressly abrogated by Congress. The court rejected the argument noting that the indictment alleged that the tribes did not actually set the rates, but that they were set by businesses controlled by Tucker. Muir also filed a motion to sever his trial from Tucker's on the grounds that he did not participate in various activities, including the development of the tribes' lending businesses. The court denied the motion, finding that Muir had not shown the likelihood of unfair prejudice. The court noted that, although Muir was alleged to have entered the conspiracy after it began, he allegedly played a role in the common scheme and participated in it with Tucker.

William Quigley, Trident Partners Ltd. – In early 2017, William Quigley, the former chief compliance officer of Trident Partners Ltd., a registered broker-dealer, was sentenced to six months in prison. [17] The sentence came after he pled guilty to charges of wire fraud and money laundering conspiracies. He also settled an SEC complaint for violating the securities laws. According to the SEC administrative order, Quigley participated with two of his brothers in the

[15] Model Rules of Prof'l Conduct R. 1.16(a)(1).

[16] *United States v. Tucker*, No. 19-CR-91(PKC), 2017 WL 3610587 (S.D.N.Y. Mar. 1, 2017).

[17] Richard L. Cassin, *Former Compliance Chief Jailed for Wire Fraud Conspiracy*, THE FCPA BLOG (Mar. 28, 2007, 11:08AM), http://www.fcpablog.com/blog/2017/3/28/former-compliance-chief-jailed-for-wire-fraud-conspiracy.html.

fraudulent offering scheme.[18] The brothers directly solicited investors abroad, purportedly telling them that their funds would be invested in "blue chip" companies and start-ups about to go public. But the funds were misappropriated by the brothers. William Quigley set up and controlled the U.S. accounts to which the investors transferred funds and from which he funneled money out. The brothers provided investors phony statements, misrepresenting the status of their funds.

C. Allegations of misrepresentations to governmental authorities

Another category of accusations against in-house counsel or compliance officers relates to alleged misrepresentations or false statements to governmental authorities. This scenario often overlaps with the previous one in that the prosecution's case is directed at an alleged conspiracy involving others, but the particular action that brings the lawyer into it involves statements or representations to authorities. Thus the ethics rules discussed already also are relevant here.

But perhaps more centrally, this scenario implicates the ethics rules relating to truthfulness as well as to confidentiality. Model Rule 3.3 deals with "candor toward the tribunal." Among other requirements, it prohibits a lawyer from knowingly making "a false statement of fact or law to a tribunal or fail[ing] to correct a false statement of material fact or law previously made to the tribunal by the lawyer."[19] In addition to a court and an arbitrator in a binding arbitration, a "tribunal" covers "a legislative body, administrative agency or other body acting in an adjudicative capacity."[20] The definition clarifies that "[a] legislative body, administrative agency or other body acts in an adjudicative capacity when a neutral official, after the presentation of evidence or legal argument by a party or parties, will render a binding legal judgment directly affecting a party's interests in a particular matter."[21]

Thus, while Rule 3.3 may not cover investigations by regulatory agencies, Model Rule 4.1 reaches much further. It prohibits a lawyer from knowingly making "a false statement of material fact or law to a third person."[22] It also requires a lawyer "to disclose a material fact to a third person when disclosure is necessary to avoid assisting a criminal or fraudulent act by a client," unless Model Rule 1.6 prohibits disclosure.[23]

Model Rule 1.6 is the key rule setting out a lawyer's confidentiality obligations. The Rule generally prohibits a lawyer from revealing information relating to representation of a client in the absence of informed consent. Disclosure is allowed in certain enumerated circumstances. These include when the lawyer reasonably believes that disclosure is necessary "to prevent the

[18] *William Quigley*, Securities and Exchange Commission, Admin. Proc. File No. 3-16560, *available at* https://www.sec.gov/litigation/admin/2017/33-10327.pdf.

[19] Model Rules of Prof'l Conduct R. 3.3(a)(1).

[20] *Id.* R. 1.0(m).

[21] *Id.*

[22] *Id.* R. 3.3.

[23] *Id.*

client from committing a crime or fraud that is reasonably certain to result in substantial injury to the financial interests or property of another and in furtherance of which the client has used or is using the lawyer's services."[24] The rule also allows disclosure "to prevent, mitigate or rectify substantial injury to the financial interests or property of another that is reasonably certain to result or has resulted from the client's commission of a crime or fraud in furtherance of which the client has used the lawyer's services."[25] Model Rule 1.9(c)(2) extends the same obligations with respect to information of a former client.

Examples:

Caprise Bearden, Pharmakon Pharmaceuticals. In November 2017, the former director of compliance for Pharmakon Pharmaceuticals pled guilty to charges of conspiracy to defraud the United States, of introducing an adulterated drug into interstate commerce, and of adulterating drugs.[26] The charges had resulted after Pharmakon, an Indiana compounding pharmacy, distributed various compounded drugs that were not the strength listed on the drugs' labeling. As part of her plea agreement, Bearden acknowledged that she lied to FDA inspectors during inspections conducted in 2014 and 2016. She falsely represented that Pharmakon had not received any test results showing drug potencies outside of the drug specifications. She acknowledged that she conspired to defraud the United States by obstructing the lawful functions of the FDA.

Taddeus Bereday, Wellcare, Inc. In mid-2017, Thaddeus Bereday, the general counsel and chief compliance officer of WellCare, Inc. pled guilty to one count of making a false statement to the Florida Medicaid program.[27] Wellcare operated health maintenance organizations or HMOs focused on government-sponsored programs like Medicaid. Under a Florida statute, Florida Medicaid HMOs were required to spend 80% of the Medicaid premium paid for certain behavioral health services on the provision of those services. If less was spent, the difference needed to be returned to the agency that administers the Medicaid program in Florida.

Wellcare had been charged with conspiring to defraud Florida's healthcare programs. The company entered into a deferred prosecution agreement, stipulating that, acting through its former officers and employees, it had conspired in a scheme to defraud Florida healthcare

[24] *Id.* R. 1.6(b)(2).

[25] *Id.* R. 1.6(b)(3).

[26] Press Release, Department of Justice, Office of Public Affairs, *Former Pharmacy Compliance Director Pleads Guilty to Introducing Adulterated Drugs Into Interstate Commerce and Conspiracy to Defraud the United States* (Nov. 22, 2017), *available at* https://www.justice.gov/opa/pr/former-pharmacy-compliance-director-pleads-guilty-introducing-adulterated-drugs-interstate.

[27] Press Release, Department of Justice, U.S. Attorney's Office, Middle District of Florida, *Former WellCare, Inc. General Counsel Pleads Guilty to Making a False Statement to Florida Medicaid Program* (June 28, 2017), *available at* https://www.justice.gov/usao-mdfl/pr/former-wellcare-inc-general-counsel-pleads-guilty-making-false-statement-florida.

programs of approximately $40 million. The scheme involved misrepresenting expenditure information for behavioral health care services.

After additional investigation with the company's cooperation, five Wellcare executives, including Bereday, were indicted on charges of conspiracy, making false statements and healthcare fraud. Four were found guilty in a jury trial in 2013, but Bereday had been unable to participate due to health reasons. Although his case had been scheduled for trial in 2017, he reached a plea agreement and was sentenced to six months in prison.[28] Based on WellCare's satisfaction of the requirements of the deferred prosecution agreement, including payment of $40 million in restitution, the charges against it were dismissed.

Oliver Schmidt, Volkswagen. Oliver Schmidt was the former top emissions compliance manager for Volkswagen in the United States. He was arrested in early 2017 in connection with the emissions cheating scandal involving Volkswagen diesel motors.[29] Volkswagen itself settled the charges against it by the Justice Department. It is also paying $22 billion in settlements and fines in connection with the scandal.[30] Volkswagen confirmed that it had installed software intended to be able to cheat emissions tests on 11 million vehicles worldwide. The software detected when testing was occurring and turned on pollution-control systems to limit emissions at the cost of engine performance. Those systems were not deployed on the road, resulting in discharges of nitrogen oxide at up to 40 times the allowed levels under the Clean Air Act. By the summer of 2015 regulators had become aware of the emissions discrepancy during testing and road driving of the vehicles.

In August 2017, Schmidt pled guilty to conspiracy to defraud the federal government and violate the Clean Air Act. According to the complaint against Schmidt, he participated in direct conversations with U.S. regulators and hid the use of the deceptive software from them.[31] Although he knew that the software was the reason for the discrepancy, he offered other technical reasons and excuses as reasons.

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[28] Nate Raymond, *Ex-WellCare General Counsel Gets Six Months in U.S. prison*, REUTERS, Nov. 22, 2017, https://www.reuters.com/article/us-wellcare-health-court/ex-wellcare-general-counsel-gets-six-months-in-u-s-prison-idUSKBN1DM2GC.

[29] Adam Goldman, Hiroko Tabuchi and Jack Ewing, *F.B.I. Arrests Volkswagen Executive on Conspiracy Charge in Emissions Scandal*, N.Y. TIMES, Jan. 9, 2017, https://www.nytimes.com /2017/01/09/business/volkswagen-diesel-emissions-investigation-settlement.html.

[30] Bill Vlasic, *Volkswagen Executive Pleads Guilty in Diesel Emissions Case*, N.Y. TIMES, Aug. 4, 2017, https://www.nytimes.com/2017/08/04/business/volkswagen-diesel-oliver-schmidt .html.

[31] Press Release, Department of Justice, Office of Public Affairs, *Volkswagen Executive Charged for Alleged Role in Conspiracy to Cheat U.S. Emissions Tests* (Jan. 9, 2017), *available at* https://www.justice.gov/opa/pr/volkswagen-executive-charged-alleged-role-conspiracy-cheat-us-emissions-tests; Complaint, *U.S. v. Oliver Schmidt*, Dkt. No. 1, Case No. 16-MJ-30588 (E.D. Mich. Dec. 30, 2016).

***Lauren Stevens, GlaxoSmithKline*.** Although an older example, the case of Lauren Stevens, relating to her actions as an associate general counsel of GlaxoSmithKline, is instructive. In 2010, a federal grand jury in the District of Maryland returned an indictment charging Stevens in connection with GSK's promotion of an anti-depressant drug for weight loss, a use that had not been approved by the FDA.[32] She was charged with various counts of obstruction of justice in connection with GSK's response to an FDA inquiry and investigation of its promotion of the drug, Wellbutrin, for the off-label use. In 2002, the FDA had sent a letter of inquiry to GSK asking it to provide materials relating to the promotional programs for Wellbutrin. Stevens was in charge of GSK's response to the FDA investigation and led the team responsible for gathering responsive documents and information. The government alleged that Stevens obstructed the FDA's investigation by withholding and concealing certain documents as well as falsifying or altering others. In particular, the government alleged that Stevens withheld slides used by speakers at GSK promotional events and information about compensation received by attendees. The government also alleged that Stevens signed and sent six letters to the FDA containing materially false statements regarding GSK's promotion of Wellbutrin for the off-label use.

Stevens' primary defense against the charges was based on her reliance on advice of counsel. She had received assistance from GSK in-house counsel and outside counsel from the law firm of King & Spalding in responding to the FDA inquiry. She took the position that she relied in good faith on their advice and the reliance negated the requisite intent to obstruct the FDA's investigation or make false statements. On March 23, 2011, the District Court dismissed the indictment without prejudice. The court found that the prosecutors had given erroneous and prejudicial legal advice to the grand jury with respect to the effect of a so-called advice of counsel defense.

On April 13, 2011, Stevens was indicted again on the same obstruction of justice charges. The case proceeded to trial. After the government rested its case, Stevens moved for a judgment of acquittal on the grounds that the government failed to present sufficient evidence to establish her guilt. In an oral ruling, the court granted her motion.[33] The judge noted that the government had received access to attorney-client privileged communications based on a decision by a Massachusetts magistrate judge that found the crime-fraud exception applied. Although the district court disagreed with the correctness of the decision, it found that the documents reflected a "studied, thoughtful analysis of an extremely broad request" from the FDA and "an enormous effort to assemble information and respond on behalf of the client."[34] The court observed that Stevens sought advice from numerous lawyers and made full disclosures to them. It found that her reliance on their advice negated the requisite intent element for all the charged crimes. The court concluded with a reminder that although "[l]awyers do not get a free pass to commit crimes …. a lawyer should never fear prosecution because of advice that he or she has given to a client who consults him or her, and a client should never fear that its confidences will be divulged

[32] *U.S. v. Stevens*, 771 F.Supp.2d 556 (D. Md. 2011).

[33] Tr. Transcript, *U.S. v. Stevens*, Crim No. RWT-10-694 (D. Md. May 10, 2011), *available at* http://lawprofessors.typepad.com/files/110510stevens.pdf.

[34] *Id.* at 5.

unless its purpose in consulting the lawyer was for the purpose of committing a crime or a fraud."[35]

D. Allegations of approving problematic actions or failing to prevent them

Another scenario in which in-house counsel and compliance professionals have become targets is when they sign-off on problematic conduct or fail to take action to prevent it. These scenarios potentially implicate each of the ethics rules discussed so far.

Examples:

Mark Ellison, DBSI. The former general counsel of DBSI was convicted, in the federal district court for the District of Idaho, with three other DBSI principals of securities fraud.[36] Headquartered in Idaho, DBSI primarily marketed tenant-in-common (TIC) interests in real estate. The interests were sold to investors through private placement memorandums and other marketing materials. Leading up to its bankruptcy in 2008, DBSI represented to investors that it was profitable, well capitalized, and had a business model that minimized risk and paid fixed returns. The government presented evidence of the falsity of these representations.

In denying his post-trial motions, the district court discussed Ellison's involvement.[37] As general counsel, he was responsible for regulatory compliance, including regulations applicable to the TIC offerings. The court noted that he "had authority over the language contained in" the materials distributed to investors. He had also been warned by DBSI's accountants about a problem in the way the company's net worth had been derived. When he was asked by sales managers to provide information about financial performance of the underlying investments, he claimed that he could not convince the CEO to make it available, either internally or to broker-dealers. He personally reviewed a profitability statement and "did not prevent it from being distributed to broker-dealers" despite knowing of the undisclosed lack of profitability.

In 2014, Ellison received a sentence of 60 months in prison. At sentencing, the judge found that the defendants were responsible for losses of more than $100 million with more than 250 victims of the fraud.

John D. Telfer, Windsor Street Capital. In early 2017 the SEC filed an administrative complaint against Windsor Street Capital, a brokerage firm, and its former anti-money

[35] *Id.* at 9-10.

[36] Press Release, Department of Justice, U.S. Attorney's Office, District of Idaho, *DBSI Founders Douglas L. Swenson and Mark A. Ellison Sentenced for Defrauding Thousands of Investors* (Aug. 20, 2014), *available at* https://www.justice.gov/usao-id/pr/dbsi-founders-douglas-l-swenson-and-mark-ellison-sentenced-defrauding-thousands-investors.

[37] *U.S. v. Swenson*, No. 13-CR-00091(BLW), 2014 WL 4071034, at *5 (D. Idaho Aug. 15, 2014).

laundering (AML) officer, John Telfer.[38] The complaint alleged that the brokerage violated the Securities Act of 1933 by facilitating the unregistered sale of penny stock shares, without adequate due diligence. The complaint also alleged violations of the Securities Exchange Act of 1934 due to the firm's failure to file Suspicious Activity Reports ("SARs") with the Treasury Department's Financial Crimes Enforcement Network (FinCEN). According to the complaint, Telfer failed to file the SARs for $24.8 million in suspicious transactions. Some of those transactions occurred in accounts of penny stock promotors who had settled separate SEC charges that they ran a "pump-and-dump" operation. As the brokerage's AML officer, Telfer was personally responsible for monitoring transactions. The SEC claims that by failing to carry out his duties, Telfer aided, abetted, and caused the brokerage's securities violations.

In June 2017, Telfer settled the SEC's allegations.[39] He agreed to be barred from the securities industry and to pay a $10,000 penalty. He neither admitted nor denied wrongdoing.

Thomas E. Haider, MoneyGram International, Inc. In May 2017, the U.S. Attorney's Office for the Southern District of New York and the Financial Crimes Enforcement Network (FinCEN) announced the settlement of a civil enforcement action filed against Thomas E. Haider, the former Chief Compliance Officer of MoneyGram International, for violations of the Bank Secrecy Act (BSA).[40] According to the complaint, MoneyGram operates a money transfer service that enables customers to transfer money from one location to another through a global network of independently-owned outlets.[41] The complaint alleged that Haider had failed to perform various obligations of a chief compliance officer. As part of his settlement, Haider admitted failing to take various actions, including failing to terminate specific outlets after receiving information that strongly indicated they were involved in consumer fraud schemes and failing to implement a policy for terminating such outlets. He also admitted failing to structure MoneyGram's anti-money laundering (AML) program in a manner that would ensure filing of Suspicious Activities Reports (SARs) with FinCEN. According to the complaint, under the BSA and is implementing regulations, a money transmitter, like MoneyGram, was required to implement and maintain an effective AML program. It was also required to file SARs with FinCEN when it knew, suspected, or had reason to suspect that certain transactions involved use of its money transfer system to facilitate criminal activity.

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[38] *Windsor Street Capital, L.P.*, Securities and Exchange Commission, Admin. Proc. File No. 3-16560, *available at* https://www.sec.gov/litigation/admin/2017/33-10293.pdf.

[39]Cara Mannion, *Ex-Exec, SEC Settle Suit Over Pump-And-Dump Reporting*, LAW360, June 14, 2017, https://www.law360.com/articles/934553/ex-exec-sec-settle-suit-over-pump-and-dump-reporting.

[40] Press Release, U.S. Dept. of the Treasury, Financial Crimes Enforcement Network, *FinCEN and Manhattan U.S. Attorney Announce Settlement with Former MoneyGram Executive Thomas E. Haider* (May 4, 2017), *available at* https://www.fincen.gov/news/news-releases/fincen-and-manhattan-us-attorney-announce-settlement-former-moneygram-executive.

[41]Complaint, *U.S. Dept. of the Treasury v. Haider*, 14-CV-9987 (S.D.N.Y. Oct. 16, 2014), *available at* https://www.justice.gov/sites/default/files/usao-sdny/legacy/2015/03/25/Haider%2C%20Thomas%20Complaint.pdf.

The original complaint sought a $1 million penalty against Haider and to enjoin him from being involved with any financial institution for a term to be determined. As part of his settlement, Haider agreed to a $250,000 penalty and a three-year injunction barring him from performing a compliance function for any money transmitter.

2. Requirements and options for in-house counsel under the ethics rules when business associates engage in unlawful conduct

The foregoing examples include ones in which in-house counsel could be viewed as having actively joined in illegal conduct of others at their client organization. Some of the other examples may have largely entailed inaction by counsel. In both scenarios, the attorneys themselves became law enforcement targets. What other options do the ethics rules allow or even require when an attorney learns that organizational clients are about to violate or have violated the law?

When the misconduct is anticipated or is ongoing, the ethics rules impose certain obligations on in-house counsel. As already noted, Model Rules 1.2(d) and 1.13(b) impose specific obligations on attorneys in this situation. The former prohibits an attorney from assisting in criminal or fraudulent conduct. The latter generally requires what is often referred to as "reporting up the ladder" when an attorney "knows" that someone in the organization intends to violate a legal obligation to the organization or intends illegal conduct likely to cause substantial injury to the organization. Under the Model Rules' definitions, "knows" refers to "actual knowledge of the fact in question" and a "person's knowledge may be inferred from circumstances."[42] The comment on Rule 1.13 cites this definition to observe that "a lawyer cannot ignore the obvious."[43]

But what if reporting up the ladder does not resolve the situation? If continued work for the client "will result in violation of the rules or other law," Model Rule 1.16(a)(1) requires withdrawal. Thus, if continuing to perform the attorney's normal duties would necessarily entail assisting criminal or fraudulent conduct, as prohibited by Rule 1.2(d), or otherwise violate the law, Rule 1.16(a)(1) calls for withdrawal. As the comment to the rule clarifies, if a client suggests a problematic course of conduct, such a suggestion does not require withdrawal. But if the client demands that the lawyer engage in conduct that would violate the ethics rules or the law, withdrawal is necessary. In the case of in-house counsel, withdrawal likely means resigning from the job. In relevant part, Rule 1.13(e) requires one other notice if withdrawing under these circumstances. It provides that the lawyer must "proceed as the lawyer reasonably believes necessary to assure that the organization's highest authority is informed" of the withdrawal.[44]

If reporting up the ladder does not result in resolving what "is clearly a violation of law" and the attorney "reasonably believes that the violation is reasonably certain to result in substantial injury to the organization," Rule 1.13(c) allows—but does not require—further

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[42] Model Rules of Prof'l Conduct R. 1.0(f).

[43] Comment on Model Rules of Prof'l Conduct R. 1.13.

[44] *Id.* R. 1.13(e).

disclosure. The rule allows disclosure even if prohibited by the confidentiality provisions of Model Rule 1.6. However the disclosure is allowed, "only if and to the extent the lawyer reasonably believes necessary to prevent substantial injury to the organization."[45] Subsection (d) confirms that subsection (c) does not apply to information stemming from the attorney's involvement in investigating or defending against an alleged violation of law.

In addition, while Rule 1.16(a)(1) requires withdrawal if representation "will result" in a violation of the rules or law, Rule 1.16(b) permits withdrawal in certain circumstances. Among other reasons, an attorney may withdraw if the client "persists in a course of action involving the lawyer's services that the lawyer reasonably believes is criminal or fraudulent."[46] The comment on the rule justifies that provision with the explanation that "a lawyer is not required to be associated with such conduct even if the lawyer does not further it."[47] Thus the rules and comment seem to distinguish "assisting" criminal or fraudulent conduct as *furthering* the conduct—which would mandate withdrawal—from conduct that merely "involve[es]" the lawyer's services. An attorney may also withdraw under Rule 1.16(b) if "the client insists upon taking action that the lawyer considers repugnant or with which the lawyer has a fundamental disagreement."[48] Rule 1.16(b) allows for withdrawal for other reasons, including a catchall provision of when "other good cause for withdrawal exists."[49]

When the lawyer becomes aware of criminal or other misconduct that has already occurred, the obligations and allowances differ. For example, the rules do not mandate withdrawal, unless of course the lawyer is being asked to take some problematic action—e.g. to make false statements to a governmental authority—in a cover-up. The rules also do not permit disclosure of confidential information other than as allowed under Rule 1.6. With respect to past criminal or fraudulent conduct, the rule only allows withdrawal if "the client has used the lawyer's services to perpetrate a crime or fraud."[50]

To assist with keeping the conditions under which these various rules kick in, Appendix A provides a high-level decision tree identifying the considerations and applicable rules when an attorney learns of conduct that violates the law. Consider the potential application of these rules in the context of one final example—an instance of a general counsel's withdrawal, as described in a 2012 exposé by the New York Times of alleged widespread bribery by representatives of Wal-Mart in Mexico:[51]

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[45] *Id.* R. 1.13(c).

[46] *Id.* R. 1.16(b)(2).

[47] Comment on Model Rules of Prof'l Conduct R. 1.16.

[48] Model Rules of Prof'l Conduct R. 1.16(b)(4).

[49] *Id.* R. 1.16(b)(7).

[50] *Id.* R. 1.16(b)(3).

[51] David Barstow, *Vast Mexico Bribery Case Hushed Up by Wal-Mart After Top-Level Struggle*, N.Y. TIMES, Apr. 21, 2012, http://www.nytimes.com/2012/04/22/business/at-wal-mart-in-mexico-a-bribe-inquiry-silenced.html.

Maritza Munich, Wal-Mart International. According to the Times piece, Munich was the former general counsel of Wal-Mart International. In September, 2005, she received a message from a Mexican executive, Sergio Cicero Zapata, alleging widespread bribery in connection with obtaining permits for Wal-Mart stores in Mexico. She commenced an inquiry, hiring an outside lawyer to debrief the executive. She sent detailed memos describing the debriefing to senior management, including Wal-Mart's general counsel, its top internal auditor, and the chief executive for Latin America. Cicero's accounts implicated many of Wal-Mart de Mexico's top brass. Although Wal-Mart initially hired an outside law firm, the firm recommended an extensive investigation. Wal-Mart executives rejected the approach and decided its lawyers would supervise a preliminary inquiry by in-house investigators. Those investigators, one of whom was a former FBI special agent, concluded that there was "reasonable suspicion" that Mexican and US laws had been violated. They found a paper trail of suspect payments totaling more than $24 million. They proposed a more thorough investigation. In the midst of a debate over next steps, Ms. Munich submitted her resignation, effective February 1, 2006. In one of her final memos she advocated expanding the investigation and warned against meddling in the investigation by implicated executives. At that point Mexican executives had already attempted to insert themselves into the investigation. Soon after Munich's departure, a decision was made to transfer the investigation to the general counsel in Mexico, someone who had himself been a target in the initial investigation. After a few weeks, he concluded that there is "no evidence or clear indication" of bribery.

Following the New York Times account, the Department of Justice launched a probe into potential violations of the Federal Corrupt Practices Act. After a three-year investigation, in 2015, media sources reported the unlikelihood of any criminal charges against Wal-Mart executives.[52] Earlier this year, Wal-Mart was reported to be close to settling the investigation by paying $300 million, an amount far below the payment previously sought by the government.[53]

The New York Times piece does not explicitly discuss Munich's reasons for resigning. But the memo she sent just before she left reflects a belief in the impropriety of the course of action being deliberated and that was subsequently implemented. The Times' article makes an excerpt of the memo available, which includes the following paragraph:

> The wisdom of assigning any investigative role to management of the business unit being investigated escapes me. Given the serious nature of the allegations, and the need to preserve the integrity of the investigation, it would seem more prudent to develop a follow-up plan of action, independent of WALMEX management participation, and that

[52] Alexandra Starr, *Wal-Mart Executives Unlikely to Be Charged Over Alleged Bribes in Mexico Report Says*, NPR, Oct. 19, 2015, 6:48 PM, https://www.npr.org/sections/thetwo-way/2015/10/19/450031690/wal-mart-executives-unlikely-to-be-charged-over-alleged-bribes-in-mexico-report.

[53] Tom Schoenberg, *Wal-Mart Close to Resolving Bribery Probe for $300 Million*, BLOOMBERG, May 9, 2017, https://www.bloomberg.com/news/articles/2017-05-09/wal-mart-said-close-to-resolving-bribery-probe-for-300-million.

> includes external legal advise [*sic*] and professional, independent investigative resources.[54]

The obligations to report up the ladder and/or to withdraw, if warranted by the circumstances, may be relatively easy to describe. But deciding when they kick in, and actually following through with them in practice, may be a lot harder. Reporting up may require an in-house attorney to go over the heads of people with whom the attorney regularly interacts, making for an uncomfortable work environment. Withdrawing entails the obvious hardships of giving up a job. Both could have implications for the attorney's future professional path. But as many of the examples described in this piece show, the path of least resistance—of going with the flow—may create the possibility of personal liability. That option also raises a question of compliance with one other ethics rule—Model Rule 2.1. That rule requires a lawyer to "exercise independent professional judgment and render candid advice."[55]

[54] Barstow, *supra* note 29.

[55] Model Rules of Prof'l Conduct R. 2.1.

Appendix A - Applicable Model Rules When Lawyer Learns of Conduct that Violates Law