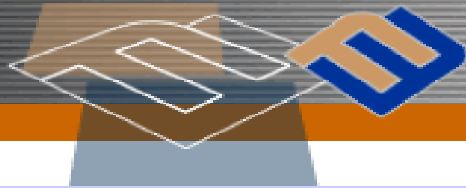


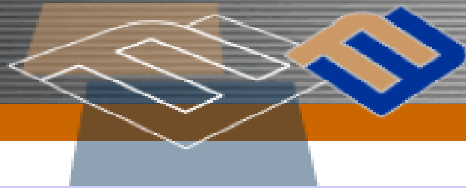
# **Overview – Securities Law and Corporate Governance Developments in the Wake of Enron**

Fenwick & West LLP  
March 21, 2002



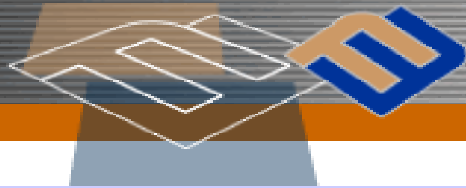
# Regulatory Focus Post Enron

- **Enron has precipitated a blizzard of SEC and other governmental statements about press releases, enhanced MD&A disclosure and proposed new corporate disclosure and accountability requirements**



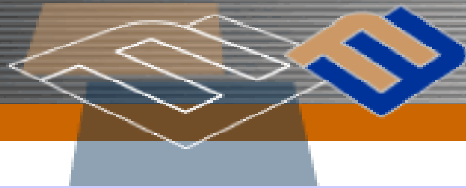
# Key Focus Areas

- **Panel One:** New disclosure requirements
  - Enhanced MD&A disclosures
  - New guidance on using pro forma presentations
  - New corporate disclosure and accountability rule proposals
  - New equity plan disclosures
- **Panel Two:** Audit committees
  - Reevaluation of audit committee duties and best practices
  - Special investigations



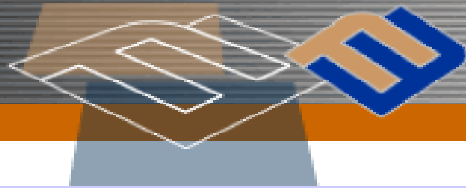
# SEC Focus on MD&A Issues

Fenwick & West LLP  
March 21, 2002



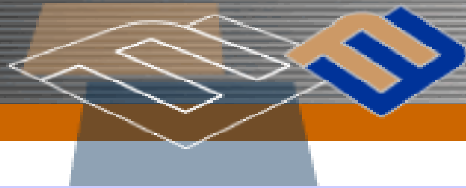
# BACKGROUND

- **Requirements of MD&A set forth in Regulation S-K Item 303 and incorporated into 10-Ks and 10-Qs**
- **Key requirements underlying recent SEC focus are the obligations to disclose in MD&A**
  - **“Known material trends, favorable and unfavorable, in the registrant’s capital resources”**
  - **“Known trends or uncertainties that have had or that the registrant reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations”**



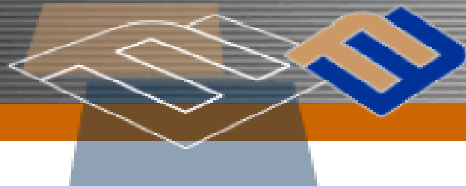
# MD&A Requirements Have Not Been Changed

- For the record, no change in MD&A disclosure requirements - the SEC's releases are couched in terms of *reminders* and *suggestions*.
- However, SEC is expanding its review of periodic filings and there is every expectation they will require the “suggested” disclosure.



# Two MD&A Releases

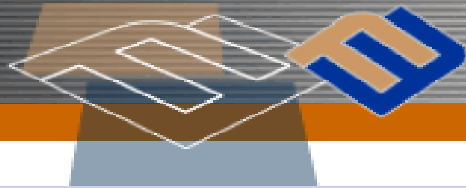
- **December 12, 2001 release: disclosure about critical accounting policies**
- **January 23, 2002 release: “sensitive financial disclosures” about liquidity, trading in non-exchange traded contracts and related party transactions**



# Critical Accounting Policies

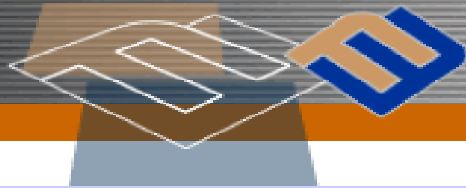
- **Companies should identify their “critical accounting policies” and be able to justify their quality and reasonableness**
- **Disclose:**
  - **effects of critical accounting policies applied**
  - **judgments made in application of critical accounting policies**
  - **likelihood of materially different results if different assumptions or conditions were to prevail**
- **Audit committees should review the selection, application and disclosure of critical accounting policies**





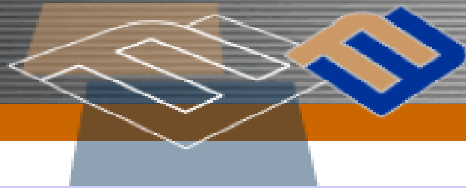
# **Sensitive Financial Disclosures**

- **Liquidity and Capital Resources**
  - **Liquidity**
  - **Off-Balance Sheet Arrangements**
  - **Contractual Obligations and Commercial Commitments**
- **Trading Activities That Include Non-Exchange Traded Contracts Accounted For at Fair Value**
- **Effects of Related Party Transactions**



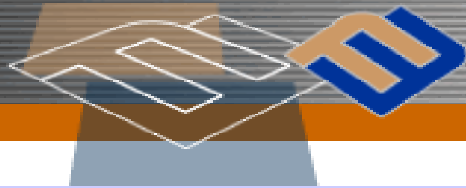
# Emerging Practices – Critical Accounting Policies

- **Most companies are including a separate MD&A section on critical accounting policies and addressing a small number of these policies.**
- **Disclosures identify critical policies and their implementation but provide little, or very general, sensitivity analysis.**
- **Most commonly cited policies include revenue recognition, valuation of long-lived and intangible assets and goodwill and valuation allowances (accounts receivable, warranties, etc.)**



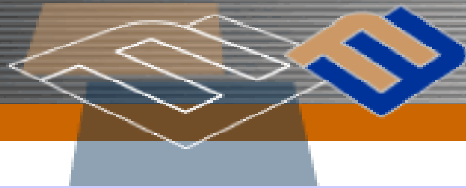
# Emerging Practices – Sensitive Financial Disclosure

- **The requirement for these disclosures is dependent on the facts and circumstances of each respective company**
- **Significant number of companies are including contractual commitment charts in MD&A**
- **Off balance sheet financing arrangements are being disclosed**
- **Non-exchange traded contracts and related party transactions are less common and we have seen few disclosures**



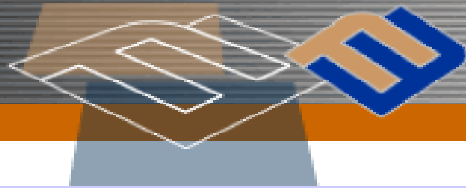
# SEC Focuses on Pro Forma Disclosures

Fenwick & West LLP  
March 21, 2002



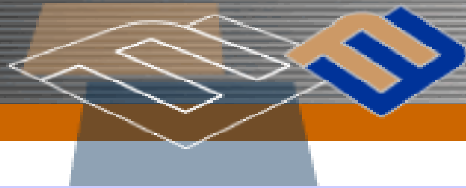
# SEC Focused on Pro Forma Disclosures

- **Concern that some pro forma disclosures are misleading**
  - Release 33-8039
  - Trump Hotels & Casino Resorts enforcement action
- **Have encouraged companies to follow NIRI/FEI guidelines**



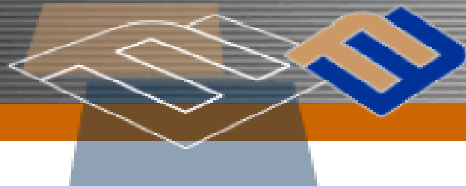
# Pro Forma Best Practices for Press Releases

- **Always include GAAP results in the release and provide generally equivalent commentary on GAAP results as is given to pro forma results**
- **Clearly label “pro forma” items as such and present the material in a fashion that minimizes the likelihood of confusing pro forma and GAAP numbers**



# Pro Forma Best Practices for Press Releases

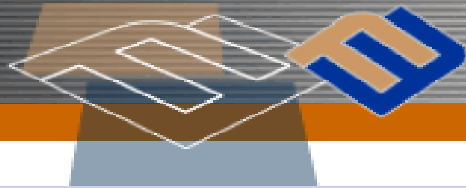
- **Provide clear reconciliation to GAAP, preferably in tabular format**
- **Describe pro forma adjustments in plain English and avoid referring to them as “non-recurring” [SEC prefers “unusual”]**



# Pro Forma Best Practices for Press Releases

- **Be careful about including pro forma disclosures in headlines and adequately explain if included**
- **Must have a reasonable basis for the pro forma adjustments made, they must be applied consistently from period to period and unusual items that positively impact results must be treated similarly to those that negatively do so**

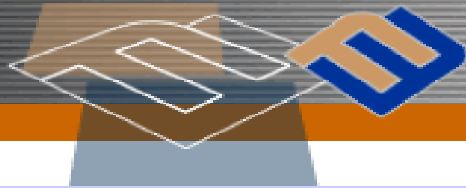




# Pro Forma Best Practices for Press Releases

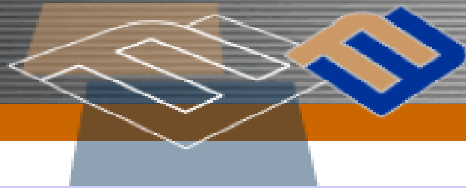
- **Include warning about investor reliance on pro forma disclosures, such as:**

**“The following pro forma supplemental financial information is presented for informational purposes only, as an aid to understanding the company’s operating results. This pro forma information is not prepared in accordance with generally accepted accounting principles and should not be considered a substitute for the historical financial information presented in accordance with GAAP. The pro forma measures used by the company may be different from pro forma measures used by other companies.”**



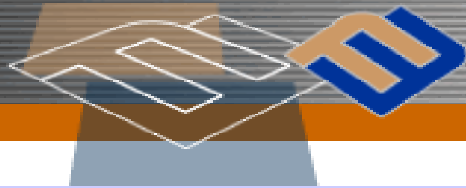
# Pro Forma Issues for 1934 Act Reports and Registration Statements

- **Recently, SEC has in certain cases required inclusion of pro forma information in 1934 Act reports and registration statements**
  - **Has caused delay of effectiveness of registration statement**
  - **Creates additional liability for company for these disclosures**



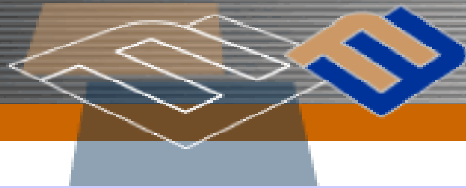
# Pro Forma Issues for 1934 Act Reports and Registration Statements

- **When including pro forma disclosures in these situations:**
  - **Pro forma financial discussion should follow GAAP selected financial information or MD&A**
  - **Pro forma financial statements should not be in an operating statement or balance sheet format that mirrors GAAP presentation**
  - **Pro forma per share data may not be appropriate**



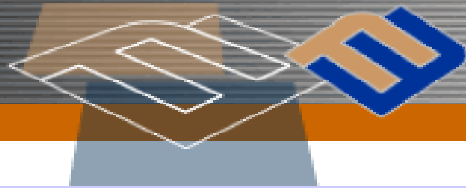
# **Focus On Corporate Disclosure and Accountability Rule Proposals**

Fenwick & West LLP  
March 21, 2002



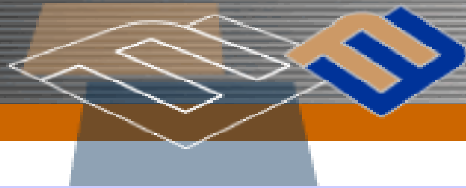
# **First Step Toward New Rules – Release 2002-22**

- **SEC taking first steps to improve financial reporting and disclosure system**
- **Expect formal proposals for these new rules by early April 2002**



# Accelerate Deadlines and Post Filings on Web

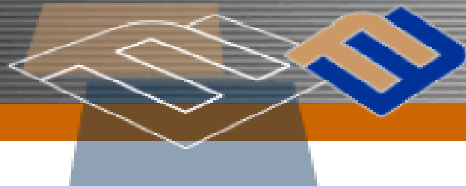
- **Form 10-K**: 60 days after year end
- **Form 10-Q**: 30 days after quarter end
- **Form 8-K**:
  - No later than second business day after occurrence of event
  - In some cases, by the opening of business the day after the event
- **1934 Act reports to be posted on company Web sites at same time as SEC filing**



# Require Current Disclosure of Additional Significant Events

**Proposed Form 8-K filing requirement for:**

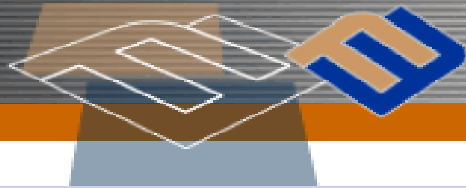
- **Defaults and other events that could trigger acceleration of obligations**
- **Transactions that result in material obligations not included in prospectus filed with SEC**
- **Offerings of equity securities not covered by prospectus filed with SEC**
- **Waivers of corporate ethics and conduct rules for officers, directors and other key employees**
- **Material modifications to rights of security holders**
- **Departure of CEO, CFO, COO or president**



# Require Current Disclosure of Additional Significant Events

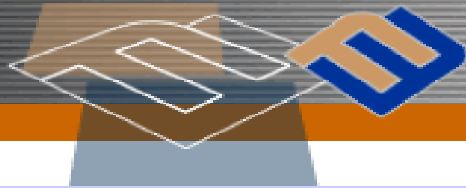
- Notices that reliance on a prior audit no longer permissible or that auditor will not consent to use of its report in registration statement
- Definitive agreement that is material to company
- Any loss or gain of a material customer or contract
- Any material write-offs, restructuring or impairments
- Any material change in accounting policy or estimate
- Changes in rating agency decisions and contacts
- De-listing of company securities
- Any material events regarding the company's employee benefit, retirement and stock ownership plans





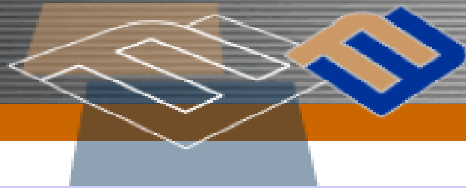
# Critical Accounting Policy Disclosures

- In MD&A include full, clear and understandable explanation of:
  - critical accounting policies
  - judgments and uncertainties affecting application of policies
  - likelihood that materially different amounts would be reported under different conditions or assumptions
- Critical accounting policies:
  - most important to portrayal of financial condition and results, and
  - require management’s most difficult, subjective or complex judgments



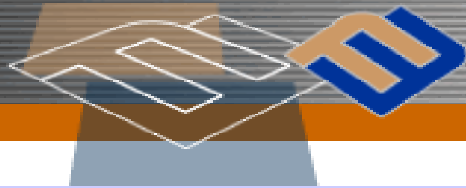
# Insider Reporting Amendments

- **Shorten dramatically Form 4 deadline**
- **Require companies (in addition to insiders) to report promptly significant stock transactions by insiders**
- **Require Form 8-K filing by companies for transactions in company's securities with insiders**



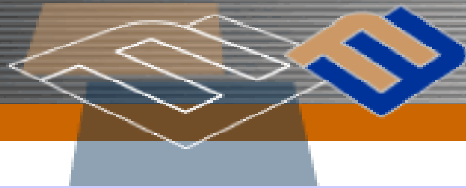
# More Rule Proposals Coming

- **Expect additional rule proposals in coming weeks and months**
  - **Nasdaq and NYSE reviewing corporate governance and listing standards, including codes of conduct and insider qualifications**
  - **Members of Congress proposing legislation**
  - **President Bush's 3/7/2002 plan to improve corporate responsibility**



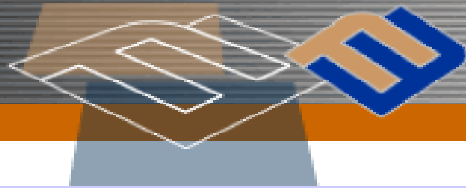
# Pres. Bush's Ten Point Plan - Disclosure

- **Better disclosures**: investors should receive true and fair picture in plain English of company's assets, liabilities and income
- **More timely disclosures**: prompt access to critical information



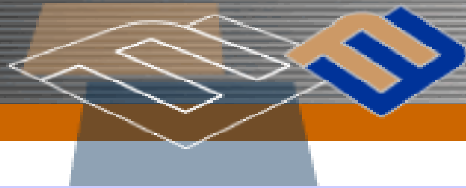
# Pres. Bush's Ten Point Plan – Insider Accountability

- **Increase CEO accountability**: personal certifications of quarterly and annual financial statements, vouching for veracity, timeliness and fairness of disclosures
- **Executive bonuses refunded**: bonuses based on financial performance should be returned to company if financials restated due to misconduct
- **Lifetime ban for misbehaving insiders**: SEC to have power to ban insiders who engage in serious misconduct from ever serving again as public company insiders
- **Quicker disclosure of insider trades**: insider trades should be disclosed within 2 days



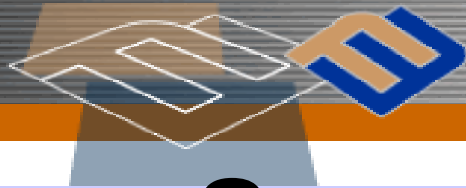
# Pres. Bush's Ten Point Plan – Enhance Audit System

- **Enhance auditor independence standards: SEC to establish more rigorous independence guidelines for outside auditors, including prohibition against outside auditor performing internal audit functions for company. SEC also to require more disclosure of fees paid to outside auditors and to require audit committee to report to investors their recommendation of outside auditors**
- **Independent regulatory board for auditing firms: to be established under supervision of SEC**



# Pres. Bush's Ten Point Plan – Enhance Audit System

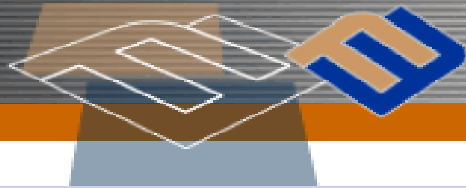
- **More SEC oversight of FASB:** SEC to exercise more effective oversight over accounting standards, including conflict of interest rules and prompt adoption of standards that reflect economic reality of transactions
- **Comparison of accounting to industry norms:** Auditors to report to audit committee how company's financial controls compare to industry norms



# Some Other Areas of SEC Rulemaking Focus

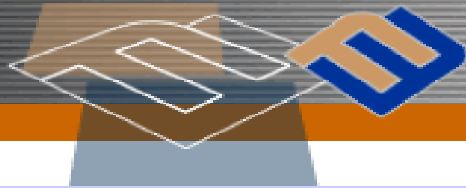
- Revisions to financial statement presentation
  - Add a summary?
  - Presentation of results in ranges?
- More clear and understandable disclosures
  - More trend information?
- Review of public and private offering process
- Rule 144





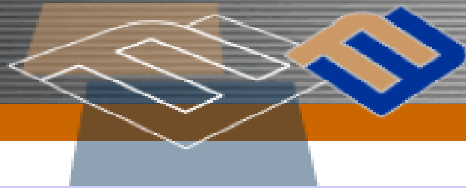
# **New Executive Compensation Disclosure Rules**

Fenwick & West LLP  
March 21, 2002



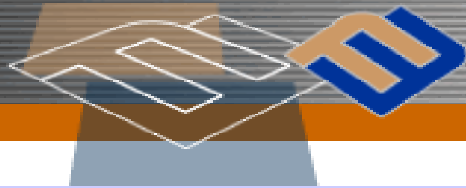
# Rationale for Change

- **Shareholders concerned about dilutive effect of equity plans**
- **Shareholders unable to obtain comprehensive understanding of option “overhang” from existing disclosures**
- **SEC and others hoped that new disclosure rules would avoid need to put in place dilution limitations**



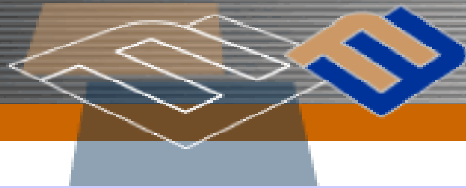
# Effective Dates

- **For 10-K disclosures**: fiscal years ending on or after March 15, 2002
- **For proxy statements**: for shareholder meetings after June 15, 2002 if taking action on an equity compensation plan



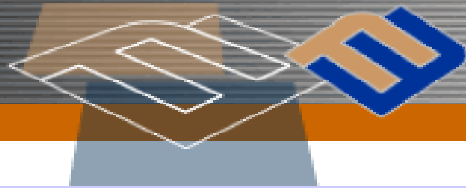
# New Tabular Disclosure Required

- **Separate categories for:**
  - **Shareholder approved plans or arrangements**
  - **Non-shareholder approved plans or arrangements**
- **Disclosures of:**
  - **Number of shares issuable upon exercise of outstanding options**
  - **Weighted average exercise price of outstanding options**
  - **Number of shares available for future grants**



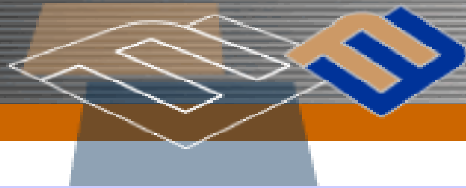
# Required Tabular Footnote Disclosures

- **Target company plans assumed in acquisition where no future grants can be made**
  - **Total assumed options outstanding and**
  - **Weighted average exercise price of those options**
- **Evergreen formulas**
- **Different classes of stock, including number of shares reserved for Rule 423 plans and restricted stock awards**



# Narrative Description of Non-Shareholder Approved Plans

- Covers “material features” of each non-shareholder approved plan
- Shareholder approved plans not required to be described by new rules
- Can cross-reference SFAS 123 footnote if it includes all required information – but requirements are different
  - SFAS 123 requires disclosures regarding shareholder approved plans
  - New rules address plans for employees and non-employees while SFAS 123 generally covers only employees
  - Material features for new rules may be broader than SFAS 123 disclosure
  - Unclear under new rules whether all individual grants must be described



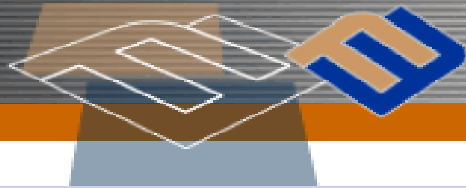
# Must File Copies of Non-Shareholder Plans

- **As exhibit to Form 10-Q or 10-K**
- **Any new plans adopted after 2/12/2002:  
next Form 10-Q (or 10-K)**
- **Existing plans not yet filed: next Form  
10-K filed for first fiscal year ending on  
or after 3/15/2002**



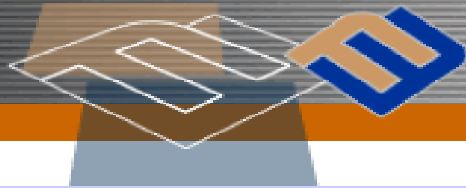
# QUESTIONS?





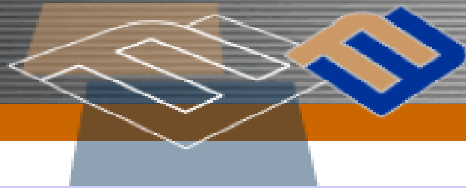
# **Audit Committee Duties and Best Practices**

Fenwick & West LLP  
March 21, 2002



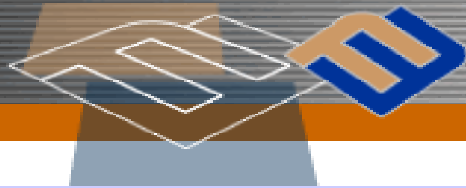
# Time to Re-Evaluate Audit Committee

- **Public and regulatory attention focused on adequacy of corporate governance**
- **Audit committee plays key role in corporate governance**
- **Now is the time to re-evaluate audit committee responsibilities and processes**



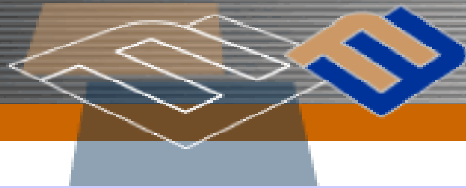
# Basic Standards of Conduct for Board

- Fiduciary duties exist under state corporate law.
- Duty of loyalty and duty of care:
  - Loyalty: act in good faith and not in furtherance of personal interests at expense of company
  - Care: take reasonable care and be prudent in managing company's affairs



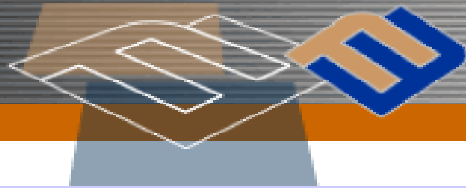
# Business Judgment Rule

- **Business judgment rule generally protects directors from fiduciary duty liability for a decision if:**
  - **Decisions are made in good faith and without self-dealing and**
  - **Directors inform themselves of all material information reasonably available prior to making decision**



# Role of Federal Securities Laws

- **Federal securities laws designed to require disclosure of information to investors.**
- **Historically, these laws were not focused on providing remedies for corporate mismanagement.**
- **However, recently SEC has focused attention on corporate governance.**



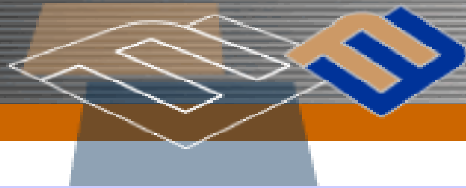
# Securities Laws Duties of Board

- SEC believes that there is an affirmative duty by the Board to aggressively fulfill responsibility to oversee the conduct and performance of management and ensure that company's public statements are candid and complete.

*In Re Cooper Companies*, Exch. Act Release No. 35082  
(12/12/94)

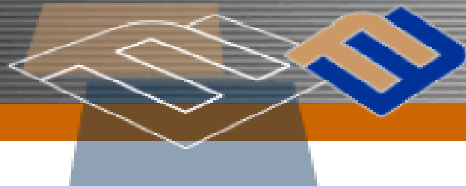
- “When an officer or director knows or should know that his company's statements are inadequate or incomplete, director has an obligation to correct the failure.”

*In the Matter of W.R. Grace & Co.*, Exch. Act Release  
No. 39157 (9/30/97)



# Liabilities under Securities Laws

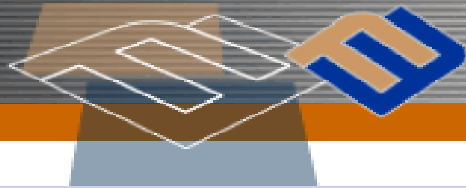
- **Registered securities offerings**: Directors are liable for material misstatements and omissions in registered securities offerings--unless due diligence defense applies.
- **Corporate communications generally**: Directors can be liable for material misstatements and omissions under Rule 10b-5 if they acted with “scienter” – knowing or intentional conduct.
  - Being reckless in failing to take steps to avoid fraud may also create liability.
- **Future legislation**: Likely in the wake of Enron.



# Failure to Meet Minimum Standards

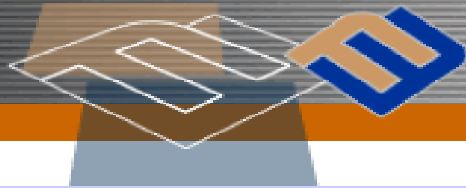
- **Can result in company and director liability:**
  - **SEC enforcement proceeding**
  - **Shareholder derivative action**
  - **Class action under federal securities laws**
  - **Criminal prosecution**





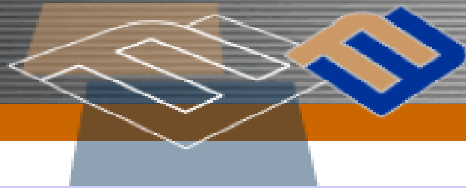
# Principal Functions and Goals of Audit Committee

- **Functions:**
  - Monitor adequacy of accounting and financial reporting processes and internal controls
  - Evaluate independence and performance of outside auditors
- **Goals (per The Blue Ribbon Committee):**
  - Deter fraud
  - Anticipate financial risks
  - Promote accurate, timely and meaningful financial reporting to Board, public and SEC



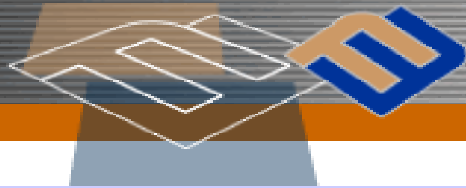
# **Governance Role of Audit Committee**

- **Audit committee helps Board satisfy its duty of care re adequacy of company's financial reporting processes**
  - **Audit committee oversees and monitors implementation of accounting and financial processes that will provide the company, the Board and the committee with adequate information to make informed judgments.**



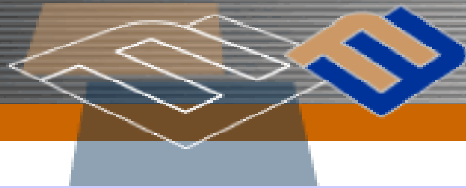
# Disclosure Role of Audit Committee

- **Audit committee helps Board comply with federal securities laws by overseeing conduct and performance of management re financial statement preparation and financial disclosures.**
- **Given their additional responsibilities and access to information, audit committee members may be held to higher standards than other outside directors in connection with fraud claims under federal securities laws.**



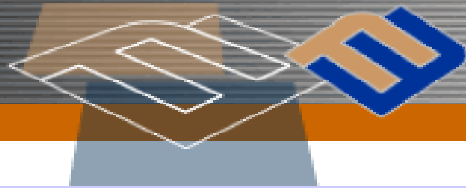
# Additional Roles of Audit Committee

- **Oversee implementation of policies designed to prevent violations of law or internal policies**
- **Conduct investigations into possible violation of law or internal policies**
- **Take steps to remedy violations of the law or internal policies where violations are known or should be known**



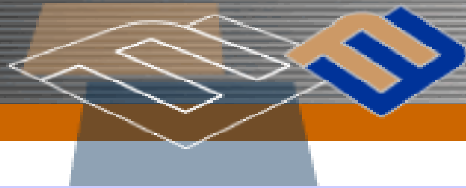
# Composition of Audit Committee

- NYSE or Nasdaq standards of “independence”
- All must be financially literate
- One must have finance/accounting background
- Should also:
  - Be prepared to devote significant time
  - Be willing to ask management and outside auditors probing questions and persist in getting answers
- Company should consider appropriate compensation and extent of protection from potential personal liability.



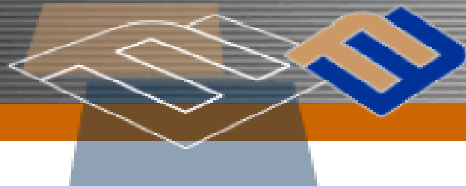
# Developing Best Practices

- **Will differ from company to company – must tailor to address each company’s circumstances**
- **Some tasks are required by SEC, Nasdaq or NYSE**
- **Others represent recommended practices to achieve goals of committee and minimize exposure of members and Board to liability**



# Best Practices – Meetings

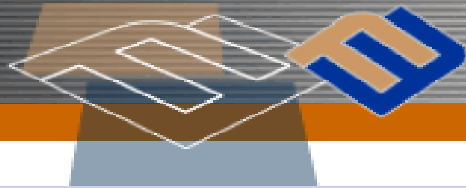
- **Quantity and quality of meetings with management, internal and outside auditors:**
  - **At least once per quarter prior to earnings release**
  - **Schedule meetings well in advance of releases**
  - **Provide written materials in advance of meeting**
  - **Allow adequate time for each meeting**
  - **Document meetings with minutes**
  - **Meet separately with auditors and management**
  - **Foster open communication**
  - **Include education component**



## Best Practices – Review of Financials

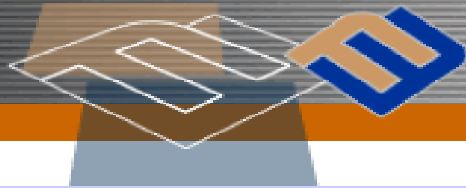
- **Review and discuss financial statements before they are released and review Forms 10-Q and 10-K (especially MD&A) before they are filed with SEC**
  - **Review the company’s business, overall business environment, risks, competitive position and strategy**
  - **What are others saying about the company, its competitors and its industry (e.g., analysts, the press and competitors)?**
  - **Did the company achieve planned results?**
  - **What is the company’s liquidity situation?**
  - **Were there any related party transactions?**
  - **What significant events or unusual transactions occurred during quarter? Late in the quarter?**
  - **What significant legal issues is the company facing?**





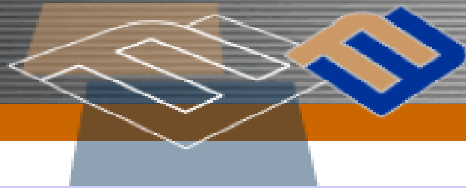
# Best Practices – Accounting Policies

- **Review and discuss accounting policies:**
  - Standards for and compliance with revenue recognition, and other key accounting policies
  - New or changed policies
  - Estimates and judgments made by management
  - Company’s position relative to industry norms
  - How is “materiality” determined
  - Other significant or unusual accounting matters, such as restructuring, reserves, acquisitions, impairment assessments, contingent liabilities and accounting for debt and equity



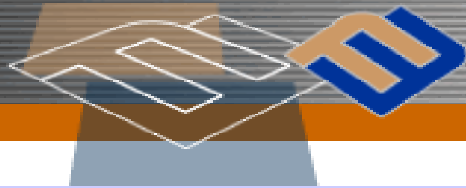
# Best Practices - Administration

- **Assess risk of fraudulent reporting**
- **Periodically review duties and performance of audit committee**
  - **Whether enumerated responsibilities are appropriate**
  - **Whether and how well committee is fulfilling them**
  - **Financial literacy tests?**
- **Review and address issues raised in outside auditors' annual management letter**
- **Assess role of audit committee in monitoring compliance with company's code of ethical conduct**
  - **Should committee assume these responsibilities?**
  - **Review of related party transactions?**



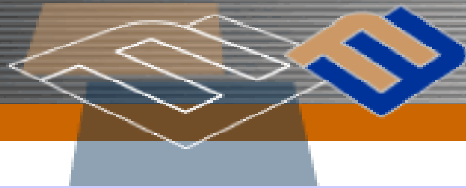
# Best Practices – Question Auditors

- **Meetings with outside auditors**
  - Before quarterly earnings are released and after auditors' SAS 71 review
  - Quality, completeness and clarity of disclosures
  - Accounting approach as conservative, moderate or aggressive; comparison to industry norms
  - SAS No. 61 matters (e.g., impact of significant transactions, audit adjustments, disagreements with management, difficulties performing review/audit)
  - Adequacy of internal controls and reporting processes
  - Inquire about adequacy of time spent on areas of greatest risk and that require most judgment



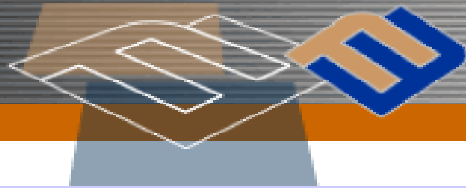
## **Best Practices – Auditor Selection**

- **Participate in retention, review and discharge of outside auditors**
  - **Review estimated and actual fees**
  - **Discuss scope of work**
  - **Inquire about adequacy of staffing, experience levels and qualifications**
  - **Communicate about relationship, responsibilities and authority of committee, management and outside auditors**
  - **Evaluate independence of outside auditors**



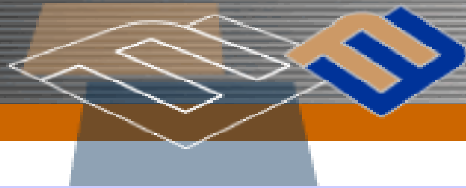
# Best Practices – Auditor Independence

- **Monitor independence of outside auditors**
  - Obtain written disclosures of all relationships
  - Consider requiring pre-approval by audit committee of non-audit services provided by outside auditors (or those above a specified dollar threshold)
  - Inquire about manner of compensation of audit partner (i.e., is compensation based in part on non-audit services)
  - Discuss and evaluate independence issues, including amount of fees billed for IT services and other non-audit services and whether these services/fees are compatible with independence



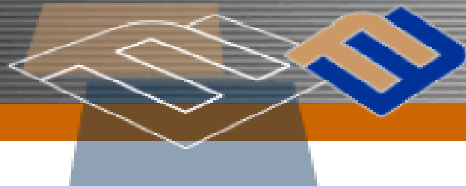
# Some Other Best Practices

- **Monitor the internal audit function**
- **Assess qualifications and performance of management**
- **Monitor adequacy of internal controls and reporting processes**
- **Prepare annual audit committee report for proxy statement**
- **Ensure ability to conduct special investigations within scope of duties and hire outside counsel/experts**



# Warren Buffet's Three Audit Committee Questions

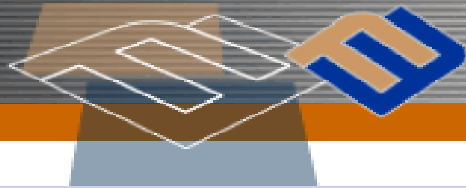
- **If the outside auditor were solely responsible for preparation of the company's financial statements, would they have been prepared in any way different from the manner selected by management?**
- **If the outside auditor were an investor, would he have received the information essential to a proper understanding of the company's financial performance during the reporting period?**
- **Is the company following the same internal audit procedure that would be followed if the auditor himself were a CEO? If not, what are the differences and why?**



# 15 More Questions To Ask

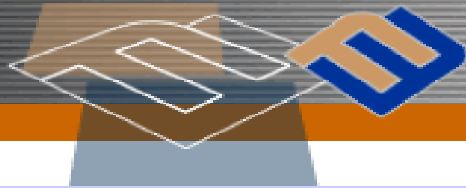
- **How much revenue was booked in last two weeks of the quarter?**
- **What were the 10 largest transactions?**
- **Were there any reciprocal or barter transactions?**
- **Were there any transactions with related parties or parties in which the company has an equity interest?**
- **Were there any activities during the quarter that moved revenues or expenses from one quarter to another?**





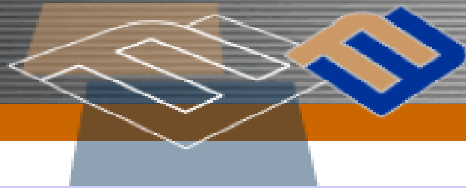
# 15 More Questions To Ask

- **What is the receivables aging pattern?**
- **Is there any deferred revenue? What is backlog?**
- **How are sales/shipments documented?**
- **Do customers have acceptance periods?**
- **What processes do you have in place to ensure that there will be no “side letters” with customers?**



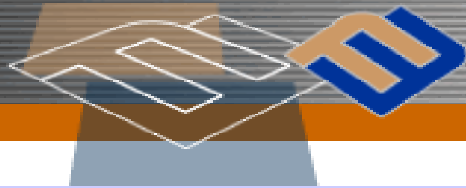
# 15 More Questions To Ask

- **How is the sales force compensated?**
- **Does the company have any equity interest or investment in any other entity?**
- **Are there any transactions that raise form over substance issues?**
- **What are the key areas where management or outside auditors make subjective judgments?**
- **What are the areas that management and the outside auditors spent the most time on?**



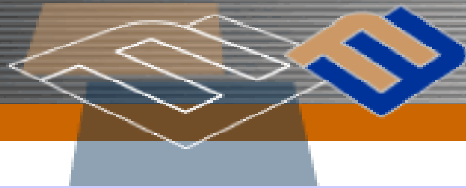
# **Audit Committee Special Investigations**

Fenwick & West LLP  
March 21, 2002



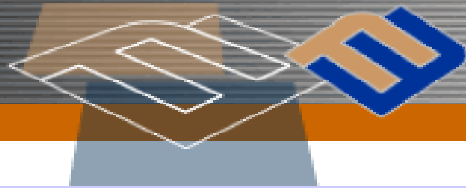
# Special Investigations - Overview

- **Common exposure areas**
- **Why an investigation may be necessary**
- **Sensitive issues**
- **Conducting special investigations**
- **Compliance programs to put in place now**



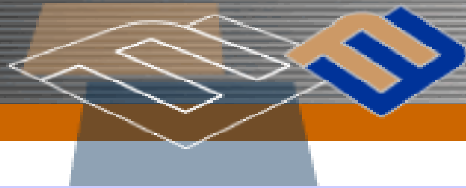
# Exposure Area – Securities Violations

- **Accounting irregularities and revenue recognition**
  - **Can lead to restatement of financials**
  - **Securities class action litigation**
  - **SEC investigation, enforcement action and/or criminal prosecution**
- **Insider trading**
- **Foreign Corrupt Practices Act**



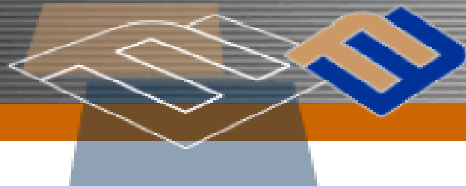
# Recent Investigations/Prosecutions

- **Accounting irregularities / restatement of earnings**
  - Enron
  - Global Crossing
  - Computer Associates
  - Homestore
  - McKesson HBOC
  - Microstrategy
  
- **Securities fraud / insider trading**
  - U.S. v. Wittenberg
  - Cal Micro Devices
  - U.S. v. Mesplou
  - Nvidia



# Should You Conduct an Internal Investigation?

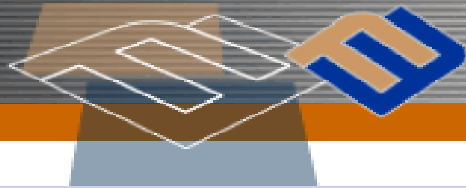
- When there is an indication of wrongdoing, the Board, Audit Committee, or management may have a duty to find out what went wrong, and what should be done about it
- Responding to potential government investigation or private litigation
- Compliance with disclosure requirements
  - Securities laws
- Duty to monitor effectiveness of compliance program/internal controls
- Advice to Board, management regarding exposure – allows proactive decision making



# Ethical Duties of In-House Counsel

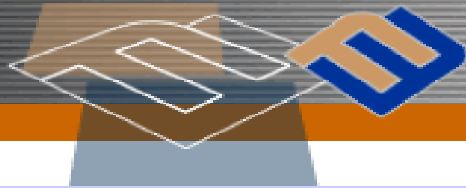
- **SEC Rule of Practice 102(e) proscribes engaging in unethical or improper professional conduct or willfully aiding securities law violations.**
  - **No definition of “improper professional conduct” is provided, but guidance is given in *In re Carter and Johnson*, Release No. 34-17597 (2/28/81)**
  - **In practice, a “go up the line” standard has evolved – an attorney who knows that an officer has failed to act on advice regarding a securities violation has a duty to go up the line, over management’s head to the Board of Directors.**
  - **Lawyer’s action must support the conclusion that he/she is exercising reasonable efforts to prevent violations, rather than capitulating to a strong willed, misguided client.**





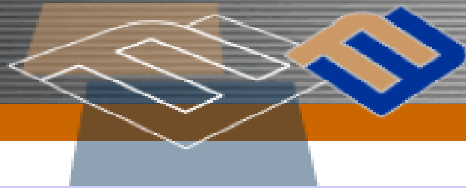
# Who Should Conduct Investigations

- **In house counsel?**
  - **May have practical conflict if high level management involved**
  - **Same concern may apply to regular corporate outside counsel**
- **Internal auditors or security**
  - **Must work at direction of counsel for work product protection**
- **Outside counsel**
  - **Do they have practical conflict with senior management?**
  - **“Vinson & Elkins” problem?**



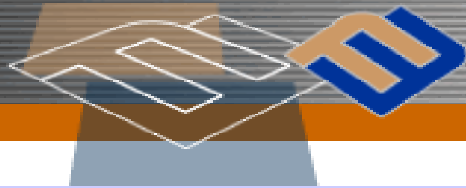
# Issues to be Sensitive to

- **Protecting the attorney-client privilege and work product protection**
- **Employee morale – minimizing disruption**
- **Employee’s privacy rights, defamation or libel, unlawful termination**
- **Duty to disclose to government agency, accountants, public**
- **Internal compliance programs**
- **Parallel criminal investigation or civil litigation**



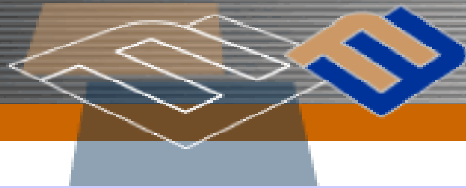
# Duty to Disclose?

- **Generally, no duty to report to the government past wrongdoing**
- **Obligation to report to government may be imposed by government contracts**
- **Disclosure to public under the securities laws (material? when must it be disclosed?)**
- **Incentives for disclosure of investigation to the government**
  - **SEC policy**
  - **Amnesty programs (antitrust)**



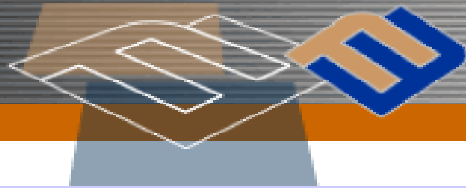
# **SEC Report on Cooperation Release No. 44969 (10/23/01)**

- **What is the nature of the misconduct, how did it arise, how high in the organization did it occur, and how long did it last?**
- **How much harm did the misconduct inflict?**
- **Who uncovered the misconduct, what steps did the Board take upon learning of it, and how long did it take to implement a response?**
- **What processes were followed to investigate, did company do thorough investigation, were the results of the investigation provided promptly to SEC?**
- **What assurances are there that the conduct is unlikely to recur, has the company changed through merger or reorganization?**



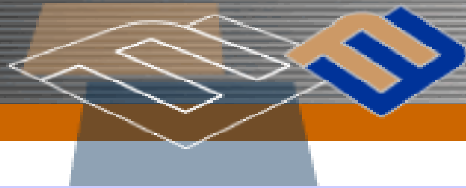
# Implementing a Compliance Program

1. **Comprehensive standards and procedures reasonably capable of reducing prospect of criminal conduct**
2. **Oversight by high level personnel**
3. **Due care in delegating substantial discretionary authority**
4. **Communications to employees must be effective to reach all levels**
5. **Reasonable steps to achieve compliance**
  - a) **Monitoring and auditing systems**
  - b) **System for reporting suspected wrongdoing without fear of reprisal**
6. **Consistent enforcement of compliance standards, including disciplinary mechanisms**
7. **Upon detection of a violation take reasonable steps to respond and to prevent further similar offenses**



# Protecting Yourself Against Privacy Claims

- **Carefully review employment agreement to determine employee's expectations of privacy**
- **Employer notice**
  - **Email monitoring**
  - **Audio monitoring**
  - **Right to search**
- **Reasonable notice provisions**
- **Obtain consent whenever possible**



# Defamation

- **Defamation claims being brought with more frequency.**
- **Couch your conclusions in terms of “opinion” rather than “fact.”**
- **Truth is best defense – carefully document your sources and interviews.**



# Questions?