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New DOJ Individual Accountability Policy

A [revised Department of Justice \(DOJ\) policy](#) serves to clarify the relationship between establishing individual accountability and qualifying for cooperation credit, particularly in the context of civil litigation.

The revised policy was announced by Deputy US Attorney General Rod J. Rosenstein in a November 29, 2018 speech. It is manifested by revisions to the United States Attorneys' Manual (now Justice Manual).

The revised policy confirms DOJ's long-standing position that "pursuing individuals responsible for wrongdoing will be a top priority in every corporate investigation." At the same time, it adopts (what appears to be) a more reasonable position with respect to a corporation's obligation to identify the individuals responsible for the wrongdoing as a condition for receiving cooperation credit.

The revised policy places greater emphasis on a good faith effort to identify individuals "substantially involved" in the wrongdoing. Particularly notable revisions allow for cooperation credit to be acknowledged in civil cases (e.g., False Claims Act) when the company identifies all wrongdoing by senior officials, including members of senior management or the board of directors. This is in contrast to the prior requirement that required identification of every person who was substantially involved in or responsible for the misconduct.

This revised policy essentially represents [the modification of the 2015 Yates Memorandum](#) to which Mr. Rosenstein first referred in several 2017 public comments. As such, the General Counsel may wish to brief the Board's Audit and Compliance Committee on how the revised policy may affect compliance program education, as well as the focus of internal investigations and other legal review activity, and the board/executive/corporation dynamic in the context of such investigations.

Can a CEO Be Too Powerful?

The public accounts of malfeasance-grounded [allegations against famed auto executive Carlos Ghosn](#) offer a series of important corporate responsibility lessons for officers and directors of health systems.

As chairman and CEO, Mr. Ghosn was one of the most powerful executives in the world, credited with guiding the success of the complex Nissan-Renault-Mitsubishi international corporate alliance. His downfall arose from an internal Nissan investigation that reportedly uncovered three primary allegations relating to personal malfeasance. *It is important to note that as of this writing, Mr. Ghosn has neither been charged with nor convicted of any legal violations.*

Mr. Ghosn has been described as a charismatic and forceful leader, celebrated for a highly efficient management style and somewhat larger-than-life nature. Such magnetic CEOs exist in most industries (including health care), albeit of different scales. Indeed, a powerful personality is often necessary to achieve exceptional corporate change and growth.

Yet the concentration of power in the hands of one person, abetted by a disenfranchised or deferential board, can become a breeding ground for executive misconduct. Notably, Nissan executives have admitted that Mr. Ghosn held too much power as chairman. Such circumstances tend to inhibit constructive skepticism and respectful dissent by the board. A confident (but still powerful) leader will embrace a board willing to challenge and disagree.

The [overarching governance lesson](#) arising from the Ghosn controversy is the strong endorsement of a basic corporate responsibility principle: as the power and influence of the CEO increases, so also must the attentiveness and engagement of the board in order to assure meaningful director oversight. This applies to all board-CEO relationships, not just to the chair/CEO of a multinational corporate alliance.

Another “Ghosn lesson” is to confirm the vitality of the organization’s internal whistleblower mechanism, for it was an internal complaint that prompted the Nissan board’s investigation. Remember that the concept of the whistleblower and “up the ladder” internal reporting has its roots in Sherron Watkins of Enron, and specific provisions of Sarbanes-Oxley.?

New Scrutiny on CEO Expense Accounts

The Ghosn controversy, with its [allegation of large, unauthorized executive expenses](#), is also prompting media and internal corporate reconsideration of CEO discretionary expense guidelines.

For example, the media has reported that Nissan made large payments towards Ghosn residences in four different cities that were allegedly not justified by business requirements, and also towards travel expenses for Ghosn family vacations. *The accuracy of these allegations have not been confirmed.* As recent *The Wall Street Journal* article noted, it is not unusual for high-profile executives to generate controversy arising from alleged expense account inconsistencies. Perceptions of expense account impropriety can often fuel whistleblower complaints.

The current circumstances are a useful prompt for the board, or a committee with delegated powers (e.g., executive compensation or audit) to revisit the continued effectiveness of its current CEO expense account policy. Indeed, the board has a particular responsibility to assure that this policy is up-to-date; achieves the needs of both the executive and the corporation; and is subject to appropriate internal reporting and other meaningful internal checks-and-balances.

Implicit in this review is a recognition that the range and nature of necessary CEO discretionary expenses evolves over time as the general business environment, the manner in which the CEO interacts with customers or other important contacts, and the related expectations of those customers and contacts, may all change. Concepts of corporate jet travel, private school payments, additional

housing allowances and family security expenses, are increasingly more legitimate in situations than they would have been in prior years.?

NYAG Audit Committee Guidelines

The recent release of [audit committee guidelines for New York nonprofits](#) underscores the increasing importance that state charity officials ascribe to the role of this key committee.

The guidelines are a detailed, nine-page, single-spaced summary of audit committee requirements and responsibilities arising from the recently (2017) updated New York Not-For-Profit Corporation Law. They were prepared by the highly regarded Charities Bureau of the state attorney general's office.

Two elements of the guidelines are broadly notable. First is the emphasis on (and definition of) independent director composition of the committee. Second is a specific, non-exclusive articulation of the duties of committee members, which focuses on a variety of matters relating to relationships with outside auditors/CPAs; oversight of tax return filings and implementation of financial controls; oversight of risk assessments and risk response plans; monitoring material legal matters; directing internal investigations as necessary; and periodic review of the organization's insurance profile.

This focus indirectly serves to prompt reconsideration by nonprofit health systems of the sufficiency of the composition and meeting schedule of the committee; as well as the practice of combining multiple important oversight tasks (e.g., compliance and risk) within the traditional responsibilities of the audit committee—especially for large, sophisticated health systems.

Note in this regard the historical willingness of the Charities Bureau to pursue breach of fiduciary duty enforcement actions against nonprofit directors, and (recently) professional advisors to nonprofits (based upon allegations of fraud).?

Board Evaluation of "Scale" in M&A Review

The Board should be mindful of the current public discourse on matters of "scale" and post-closing pricing in health care mergers.

A recent "[Special Report](#)" from [Fitch Investors](#) notes that "one of the age-old reasons to merge—to gain leverage with the payors—remains alive and well today," and that hospital mergers often serve to lower overall costs. However, a [newly published article in The New York Times](#) challenges the presumption that hospital mergers benefit consumers with cheaper prices from coordinated services and other savings. Indeed, analysis conducted for the newspaper suggests the opposite to be true in many cases; *i.e.*, that "mergers have essentially banished competition and raised prices for hospital admissions in most cases."

The Board should understand that its consideration of "scale" and "leverage" in the context of M&A evaluation is fraught with material Clayton Act Section 7 risks. [From an antitrust perspective](#), they are best applied as a basis to move the discussion to matters of "stakeholder value"; e.g., improved care, less costly care, greater access, etc. Focusing on the establishment (and achievement) of post-closing goals intended to lower costs, improve quality and increase access to care will be a more productive use of board oversight as it relates to transaction antitrust feasibility.

These factors are of special relevance given the [Federal Trade Commission's \(FTC\) November 27](#)

[announcement](#) that it would not challenge a merger between two Massachusetts hospitals, based on a settlement agreement between the hospitals and the Massachusetts Attorney General addressing issues related to health care access, including certain price caps over a period of seven years.?

Grassley Returns to Focus on Tax-Exempts?

Board committees with oversight responsibility for compliance and for mission should [note the return of Sen. Charles Grassley as Chair of the Senate Finance Committee](#).

In his previous service as Chair, Sen. Grassley was well-known for his vigilant oversight of the nonprofit sector, with a particular concentration on tax-exempt health care systems (e.g., IRC Sec. 501(r) compliance and CEO compensation). Based on recent comments, the Senator can be expected to continue this emphasis on oversight, rather than legislation.

Sen. Grassley's return to Finance Committee leadership comes at a critical time for the tax-exempt hospital sector. The Tax Cuts and Jobs Act exposed elements of Congressional concern as to when and why tax-exempt operations should appropriately be exempt from income taxation. These concerns may become enhanced with the evolution towards large, national tax-exempt organizations (in health care and other sectors).

With Senator Grassley's return to Finance Committee leadership, all tax-exempt organizations are well-advised to expend greater organizational effort to support a continued claim to tax-exempt status. This includes, at a minimum, a governing board that will be even more engaged in assuring operation of the system as a whole for exempt purposes—especially as the core health care mission evolves away from the traditional inpatient bed tower-centric operations model.?

Emphasis on Whistleblower Programs

Board oversight of whistleblower program effectiveness should be informed by several recent developments.

One such development was the [November 14 Harvard Business Review article, "Research: Whistleblowers Are A Sign of Healthy Companies."](#) This article, summarizing research conducted by the authors, argues that material whistleblower activity is "crucial to keeping firms healthy, and that functioning internal hotlines are of paramount importance to business goals including profitability." It refutes the suggestion, posited by some, that higher whistleblower activity is an indication of internal control weakness. The survey indicated that healthy whistleblower programs result in reduced exposure to litigation and costly settlements.

[Another development—from the "Ghosn controversy"](#) is media reports indicating that it was not the operation of any internal controls, but rather an internal complaint alleging a series of financial improprieties, that prompted the Nissan board's investigation of Mr. Ghosn. Indeed, Nissan reportedly had revised its whistleblower program shortly before this controversy arose.

Whistleblower mechanisms, as a component of effective legal compliance programs, are grounded in provisions of the Sarbanes-Oxley Act, the Federal Sentencing Guidelines, and in DOJ principles of prosecution of business corporations. It is essential that senior corporate leadership demonstrate the appropriate "Tone at the Top" with respect to evidencing support for effective whistleblower programs. As the *HBR* article suggests, executive goals associated with reducing the number of whistleblower reports—while perhaps well intentioned—may ultimately be counterproductive.?

More University of Louisville Foundation

[Further developments in the long running University of Louisville Foundation controversy](#)

demonstrate why it remains one of the most notorious—and thus most relevant—of recent scandals in the nonprofit sector.

The most recent development was the [November decision by the Jefferson \(Kentucky\) Circuit Court](#) denying a [motion](#) by the former President of University of Louisville and of the Foundation that the Foundation indemnify him for his legal fees incurred in defending a breach of fiduciary duty-grounded action instituted by the University and the Foundation.

The Court's ruling noted that the record failed to demonstrate that the former CEO was entitled to advancement of legal fees under the corporation's bylaws and under the business judgment rule, and that the nature of his claimed injury was not subject to injunctive relief. The ruling did leave open the possibility of reimbursement should the former president prevail in the litigation win the suit.

This entire saga has continued for several years without any public indication of state or federal investigation (beyond Internal Revenue Service scrutiny). However, the report of the forensic audit, the civil litigation between the parties and the extensive media coverage are a reminder to corporate leaders inclined to discount the legal risks of aggressive business practices: "You may avoid the result, but you won't avoid the ride."

This latest decision is also a reminder of the importance in establishing clarity in the corporate articles, bylaws and organizational policies on which parties are, or may be, entitled to indemnification, and reimbursement for (and advancement of) legal fees and expenses, and under what circumstances.?

DOJ on Effective Compliance Programs

[Recent comments by a senior DOJ official](#) provide useful guidance for the Audit and Compliance Committee on the attributes of both effective, and ineffective, compliance programs.

The comments were provided on November 28 by Principal Deputy Assistant Attorney General John P. Cronan in a presentation to the Practising Law Institute (PLI). Much of Mr. Cronan's comments focused on the importance attributed by DOJ to the existence and effectiveness of a company's preexisting compliance program in making a decision as to whether to charge a corporation. Mr. Cronan provided several examples of what he referred to as effective and ineffective programs. One such example was a global money services company that recently agreed to extend its original deferred prosecution agreement (DPA) and forfeit \$125 million due to what DOJ determined to be serious flaws in its anti-fraud and anti-money laundering programs.

According to DOJ, the company failed to maintain effective compliance programs during the course of the DPA, inadequately disclosed those weaknesses to the government, and failed to complete the enhanced compliance undertakings required by its 2012 DPA. These and other alleged compliance failures led to an extension of the original DPA and the monetary forfeiture.

Another example of ineffective compliance cited by DOJ was the failure of an international financial services company to take corrective action after initially identifying numerous corporate agents who were allegedly involved in or facilitated fraud-related transactions. The company allegedly continued to conduct business with these agents after internal recommendations that they be suspended or

otherwise disciplined. As a result of this conduct, which occurred over a period of years, the company entered into a DPA in which it agreed to forfeit almost \$600 million (and also settled a related action with the FTC).

The DOJ official also notes several examples in which voluntary disclosures by the company (involving conduct of senior executives), grounded in strong compliance programs, prompted DOJ to decline to prosecute the company, instead bringing charges against culpable individuals.?

Controversy with Advisory Board Service

[Recent allegations involving a senior Trump administration official](#) portends controversy with the scope of health system advisory board service and the protections afforded to its members.

Advisory boards are popular vehicles by which health systems can involve former board members, community leaders and influential health industry observers in the strategic direction of the system while preserving strong ties to the communities they serve. The advisory board is a particularly valuable mechanism in post-merger situations, as a way to accommodate directors who lost their seats in the combined governance structure.

Advisory directors typically have no vote, but are provided with conduits through which they may provide advice to management, and are often supported with confidential health system information from which they can provide the advice. They are usually only subject to the duty of loyalty (primarily with respect to confidentiality).

However, recent reports in national media outlets concerning the advisory board service of a senior Trump administration official may prompt questions from advisory board members on their own legal exposure, and whether they are covered by the health system's D&O insurance. The official had in the past been an advisory board member for a marketing company, which recently settled (financial payment) charges with the FTC associated with defrauding investors. According to media allegations, the official provided the FTC with untruthful responses to questions concerning his awareness as an advisory board member of the conduct that led to the charges.

Given the prominence of the official, this story has the potential to continue in the media forefront for some period of time. As a result, there may be value for the health system's governance committee, teaming with the general counsel, to proactively clarify for its advisory board membership their roles, fiduciary status and extent of D&O and related insurance coverage.

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