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U.S. Department of Justice Announces New Safe Harbor Policy for Voluntary Self-Disclosures Made in Connection with Mergers and Acquisitions

Deputy Attorney General Lisa Monaco Announces Additional Incentives for Acquiring Companies to Voluntarily Disclose and Remediate Misconduct Identified at Acquired Companies

SUMMARY

On October 4, 2023, Deputy Attorney General Lisa O. Monaco announced a new safe harbor policy providing that acquiring companies can be entitled to a presumption that the DOJ will decline to prosecute them if they make voluntary self-disclosures of potential criminal misconduct to the U.S. Department of Justice with respect to conduct identified in connection with mergers and acquisitions. The new policy, which applies to all federal criminal investigations in the United States, is the first Department-wide policy addressing voluntary self-disclosures concerning potential criminal misconduct identified in the M&A context and expands on prior policies addressing this issue, notably the Criminal Division's Corporate Enforcement Policy.

DAG Monaco stated that the new policy places "an enhanced premium on timely compliance-related due diligence and integration." In particular, to be eligible for the benefits of voluntary self-disclosure under the new policy, the acquiring entity must self-disclose criminal misconduct within six months of closing and remediate misconduct within one year.

A. BACKGROUND

The updated Principles of Federal Prosecution of Business Organizations, released in March of this year, require that all DOJ components that prosecute corporate crime maintain policies providing explicit benefits to companies that make voluntary self-disclosures in criminal cases.

The Criminal Division's Corporate Enforcement Policy, which was most recently updated in January of this year, has explicitly applied in the M&A context for several years. According to that policy, acquiring companies that voluntarily self-disclose and timely and appropriately remediate misconduct they identify at acquired companies are, absent aggravating circumstances, subject to a presumption of a declination of prosecution, with a requirement to pay all disgorgement, forfeiture, and restitution resulting from the misconduct. The Corporate Enforcement Policy specifically notes that "[t]he Criminal Division recognizes the potential benefits of corporate mergers and acquisitions," and where an acquiring company "uncovers misconduct through thorough and timely due diligence or . . . post-acquisition audits or compliance integration efforts, and voluntarily self-discloses the misconduct" and timely implements an effective compliance program at the acquired entity, there will be a presumption of a declination for the acquiring company. The policy also states that even if aggravating circumstances exist as to the acquired company (for example, the involvement of executive management in the misconduct), acquiring companies may nonetheless be eligible under the Policy for a declination.

B. SAFE HARBOR POLICY

In announcing the new Department-wide Safe Harbor Policy, DAG Monaco explained that "[e]ncouraging companies to self-report misconduct can result in a virtuous cycle: by giving a path to resolution and declination to companies trying to do the right thing, we are able to identify and prosecute the individuals who are not."

The new Safe Harbor Policy builds on the Corporate Enforcement Policy, but applies Department-wide and takes a different approach in certain key respects. Acquiring companies now have clear deadlines to self-disclose and remediate and are still eligible for the presumption of a declination in all cases involving aggravating circumstances at the acquired company provided they satisfy the requirements of the Safe Harbor Policy.

Specifically, under the Safe Harbor Policy, acquiring companies will receive a presumption of declination if:

1. The company *promptly* and *voluntarily* discloses criminal misconduct within six months from the date of closing;
2. The company *cooperates* with the ensuing investigation; and
3. The company engages in requisite, timely, and appropriate *remediation*, *restitution*, and *disgorgement*.

In order to qualify, the acquiring company must disclose the misconduct discovered at the acquired entity within six months of closing, regardless of whether the misconduct was discovered pre- or post-acquisition. And that misconduct must be fully remediated within one year from the date of closing. DAG Monaco noted that "[b]oth of these baselines are subject to a reasonableness analysis" because each transaction presents unique circumstances and considerations; for instance, more complex transactions may merit extended time frames, although misconduct "threatening national security or involving ongoing or imminent harm can't wait for a deadline to self-disclose."

DAG Monaco also noted that aggravating factors will be treated differently in the M&A context. An acquiring company's eligibility for a declination will not be impacted "in any way" by the presence of aggravating factors at the acquired entity. Similarly, unless aggravating factors exist at the acquired company, that entity can also qualify for voluntary self-disclosure benefits in the event an acquirer voluntarily self-discloses under the policy. Acquired companies with aggravating circumstances do not receive any protections under the Safe Harbor Policy, and would need to look to the self-disclosure policy of the relevant DOJ component to determine what protections may be available if its acquirer satisfies all of the requirements of the policy. Finally, any misconduct disclosed under the Safe Harbor Policy will not be factored into any future recidivist analysis for the acquiring company.

C. IMPLICATIONS

The new policy reflects a continued emphasis by the DOJ on the importance of voluntary self-disclosures in corporate criminal matters and now provides acquiring companies with clear incentives to self-disclose, cooperate, and remediate in all corporate criminal matters before the DOJ.

Perhaps responding to past criticism of reliance on more indeterminate concepts like "prompt" or "immediate" self-disclosure in the Criminal Division's Corporate Enforcement Policy, the DOJ is "doubling down on clarity and predictability" with firm deadlines. But while providing clarity and predictability, the new Safe Harbor Policy now subjects acquiring companies to strict deadlines that may not be practically attainable in many cases. In complex mergers with lengthy integration processes, and in view of the time necessary before acquired entities can be included in an acquirer's consolidated financial audit process, the clock may run out before even a diligent acquiring company becomes aware of the misconduct. Similarly, during a complex integration, one year may be insufficient to fully identify the root causes of, and remediate, misconduct. Although the policy tempers these deadlines with a "reasonableness analysis," it remains to be seen how strictly the DOJ will adhere to the six-month and one-year time frames for disclosure and remediation.

Companies will be well served to carefully evaluate the DOJ's heightened scrutiny on the role of compliance during a M&A transaction, which could function as either a shield for an acquirer if properly executed, or an inadvertent sword for the DOJ if an acquirer falls short of these heightened expectations. Acquiring companies should also consider the potential costs and benefits of designing their diligence and integration

plans with a view to identifying any potential past and ongoing misconduct promptly in order to maximize the benefits of the Safe Harbor Policy should they choose to self-disclose to the DOJ. It is also advisable to have a framework in place to evaluate whether to self-disclose to the DOJ and ensure that if an acquiring company is seeking safe harbor under the policy, it is also well-positioned to satisfy the cooperation and remediation requirements.

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