WRITTEN STATEMENT OF

VIKRAMADITYA KHANNA

PROFESSOR OF LAW, UNIVERSITY OF MICHIGAN LAW SCHOOL

BEFORE

UNITED STATES HOUSE OF REPRESENTATIVES
COMMITTEE ON THE JUDICIARY
SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW

REGARDING

HEARING ON ACCOUNTABILITY, TRANSPARENCY, AND UNIFORMITY IN CORPORATE DEFERRED AND NON-PROSECUTION AGREEMENTS

JUNE 25, 2009

Chairman Cohen, Congressman Franks, Chairman Conyers, Congressman Smith, and distinguished Members of the Subcommittee, thank you very much for inviting me to testify today at the hearing on Accountability, Transparency and Uniformity in Corporate Deferred and Non-Prosecution Agreements.

My remarks will primarily focus on corporate monitors who are often appointed to oversee behavior at firms subject to Deferred or Non-Prosecution Agreements (DPAs). In particular, I examine when it is desirable to appoint corporate monitors and methods for addressing concerns that arise with the use of monitors as sanctions. I conclude with recommendations for enhancing the institution of the corporate monitor. The discussion is largely based on the analyses in my articles on corporate monitors and on-going research in this area.[1]

My overall conclusions are that corporate monitors may be beneficial in a number of instances and that it is important to take steps to strengthen the market for their services to help assuage concerns that are already beginning to be discussed in the media and in Congress. In this statement I also put forward a series of suggestions that help to clarify when monitors are desirable and that detail what steps we can take, and have been taking, to further the development of a market for monitor services.

1. The Growth of Corporate Monitors

Over the last decade we have witnessed an increase in the appointment of corporate monitors as part of DPAs between law enforcement agencies and firms to address claims of alleged corporate wrongdoing.[2] Monitors have been appointed in a wide range of areas with often quite broad powers.[3] Further, even though most monitors have been former government enforcement officials or

---

[1] *See, e.g.*, Vikramaditya Khanna, *Reforming the Corporate Monitor?*, *in* PROSECUTORS IN THE BOARDROOM: USING CRIMINAL LAW TO REGULATE CORPORATE CONDUCT *forthcoming* (ANTHONY S. BARKOW & RACHEL E. BARKOW, EDS, 2009); Vikramaditya Khanna *&* Timothy L. Dickinson*, The Corporate Monitor: The New Corporate Czar?*, 105 MICH. L. REV. 1713 – 55 (2007); Brandon L. Garrett, *Structural Reform Prosecution*, 93 VA. L. REV. 853, 858 (2007).

[2] *See* Lawrence D. Finder & Ryan D. McConnell, *Annual Corporate Pre-Trial Agreement Update 2007*, available at: http://ssrn.com/abstract=1080263; *See* 2008 YEAR-END UPDATE ON CORPORATE DEFERRED PROSECUTION AND NON-PROSECUTION AGREEMENTS, GIBSON, DUNN & CRUTCHER LLP PUBLICATIONS, Jan. 06, 2009 [*hereinafter* Gibson Dunn]. Available at: http://www.gibsondunn.com/publications/pages/2008Year-EndUpdate-CorporateDPAs.aspx [*hereinafter* GIBSON DUNN].

[3] *See* Khanna & Dickinson, *supra* note 1 (noting use of monitors in DPAs alleging securities fraud, health care fraud, and Foreign Corrupt Practices Act violations amongst others); Khanna, *supra* note 1.

judges,[4] their tasks have been crafted quite flexibly. Indeed, in many instances important issues were left unsettled including how, if at all, could the monitor be removed, how compensation should be set, and what reports (and disclosure) should the monitor provide?[5]

The flexibility of the corporate monitor seems matched by the speed with which it was adopted.[6] In particular, the growth in monitoring assignments accelerated after the Enron series of scandals. This was due, in part, to concerns that indictments of corporate entities might lead to substantial "collateral damage" (e.g., the demise of Arthur Andersen and the effect on its employees) and that the increase in prosecutions placed a substantial strain on enforcement resources.[7] The DPAs and monitors provided a way to address both concerns by avoiding the indictment and saving enforcement resources while still being able to impose changes on the firm. Although there was little regulation of monitors and DPAs, the Department of Justice (DoJ) provided guidance in the form of a series of memos with the Thompson Memo (2003) receiving the most attention.[8]

The impressive growth and flexibility of DPAs and monitoring assignments has recently generated criticism and controversy. In particular, concerns have been raised that DPAs and monitors may be used to avoid stronger more effective sanctions, that waiving attorney-client privilege was considered a requirement before a firm could obtain a DPA, that the selection and compensation of monitors was not very transparent,[9] that monitors face limited accountability for their own behavior even though their powers to make firms accountable seem far-reaching,[10] and that there seems little independent

---

[4] Monitors are, in theory, selected by both the Department of Justice (DoJ) and the firm, but it seems the actual choice was heavily influenced by the DoJ's preferences. *See* Khanna & Dickinson, *supra* note 1.

[5] *See id.*

[6] The first corporate monitor was appointed in the 1994 *Prudential Securities* case. *See* Deferred Prosecution Agreement, United States v. Prudential Sec., Inc., No. 94-2189 (S.D.N.Y. Oct. 27, 1994), *available at* http://www.corporatecrimereporter.com/documents/prudential.pdf; *see also* SEC v. Prudential Sec., Inc., No. 93 Civ. 2164, 1993 WL 473189, at *2–3 (D.D.C. Oct. 21, 1993). Although monitors are relatively new, the use of an outside supervisor or expert as part of a resolution of enforcement proceedings has a lengthy history. *See* Khanna & Dickinson, *supra* note 1.

[7] *See* GIBSON DUNN, *supra* note 2.

[8] *See* U.S. DEPARTMENT OF JUSTICE MEMORANDUM ON PRINCIPLES OF FEDERAL PROSECUTION OF BUSINESS ORGANIZATIONS, [*hereinafter* Thompson Memo], January 20, 2003. Available at: http://www.usdoj.gov/dag/cftf/corporate_guidelines.htm. This was followed by further memos.

[9] *See* Eric Lichtblau, *In Justice Shift, Corporate Deals Replace Trials*, NEW YORK TIMES, Page A1, April 9, 2008 (available at: http://www.nytimes.com/2008/04/09/washington/09justice.html?_r=1&scp=4&sq=vikramaditya&st=cse&oref=slogin); John C. Coffee Jr., *Deferred Prosecution: Has it gone too far?*, NAT'L L.J., July 25, 2005 at 13.

[10] *See* Khanna & Dickinson, *supra* note 1.

oversight of the DPA and monitoring process. Examining these important concerns requires us to take a step back and ask – at a more general level – when is it desirable to appoint monitors and how should we oversee that process?

2. When is it Desirable to Appoint a Corporate Monitor?

As a starting point, the question of whether to have a DPA and whether to appoint a monitor are conceptually distinct questions. For example, there are DPAs that do not require monitors. Thus, the reasons to consider a DPA (e.g., to minimize collateral damage) are a necessary, but not sufficient condition for appointing a monitor.[11] To examine when a corporate monitor is desirable we need to identify the core attributes that differentiate it from the other kinds of sanctions we could use and then inquire when those attributes are desirable. Further, understanding when monitors are desirable will help us address concerns about monitors being used to avoid imposition of stronger and potentially more effective sanctions on firms.

Let us then begin with the core attributes of monitors. Monitors are appointed prior to judgment, by agreement between the government and the firm, and tend to have frequent on-going contact with the firms they are monitoring.[12] Thus, the monitor represents the imposition of a supervisor as a sanction (as compared to a cash fine) and then within the universe of possible supervisors it represents someone who provides frequent oversight. It is when these two features are desirable that a monitor may be warranted.

The first question is then when is it desirable to impose a supervisory sanction in addition to a simple cash fine?[13] After all, if the prospect of a cash fine alone would induce a firm to take compliance-enhancing measures (including hiring its own compliance experts) to reduce the chances of future wrongdoing, then there appears little need to *impose* a monitor or other supervisor. Moreover, we generally prefer using cash fines to deter wrongdoing because they are socially cheaper than relying on supervisory sanctions.[14] The social costs of cash fines are those costs involved with transferring cash from one party to the other.[15] However, the social costs of a monitor can include larger

---

[11] *See* Khanna, *supra* note 1.

[12] *See* Khanna & Dickinson, *supra* note 1.

[13] *See id.*

[14] *See id.*; V.S. Khanna, *Corporate Criminal Liability: What Purpose Does It Serve?*, 109 HARV. L. REV. 1477 (1996).

[15] *See* Khanna, *supra* note 14.

costs, such as the costs involved with a business being under supervision and the costs associated with estimating the deterrent effect of a monitor.[16] Given these higher costs we should prefer to rely on the socially less costly cash fines until their deterrence potential is exhausted and then, if greater deterrence is desired, to explore the higher costs sanctions like monitors.[17]

Generally, cash fines provide insufficient deterrence when the firm does have not enough assets to pay the desired fine or when the magnitude or effect of the desired fine is so large that it is not politically acceptable (e.g., collateral consequences become large).[18] This seems likely in at least two instances. First, as the harm caused increases it is more likely that the fine necessary for deterrence will exceed the firm's ability to pay or pass the politically unacceptable threshold. Second, recidivist corporations might, at times, merit the imposition of supervisory sanctions. For example, when a firm repeatedly violates the law because it receives large socially unacceptable gains from doing so, then it is less likely that a cash fine will obtain the desired level of deterrence.[19]

A final, but somewhat unrelated, justification is that supervisors could help to save government enforcement resources, which can then be used in pursuing other cases. The government saves resources by not having to litigate the case and by not paying the monitor (who is paid by the firm).[20]

If a supervisor sanction is preferred then the question becomes when will a supervisor with frequent on-going contact be desirable? Such contact is most valuable when the wrongdoing is difficult to detect.[21] In addition, such frequent contact provides monitors with substantial information about the firm and

---

[16] *See* Khanna & Dickinson, *supra* note 1. Compliance experts also generate benefits (e.g., reduced wrongdoing) to be weighed against their costs. However, if a monitor provides more benefits than costs for the firm, then the firm should be willing to voluntarily retain a compliance expert (as some already do). Indeed, even if firms were reluctant to voluntarily hire a compliance expert, a large cash fine might motivate them to do so rather than relying on a smaller cash fine plus the government imposing a monitor. This issue is explored in Khanna & Dickinson, *supra*, but does not significantly change the analysis presented above.

[17] *See id;* Khanna, *supra* note 14. The monitor sanction would be preferred when we desire greater deterrence than the cash fine and the net benefits of the monitor (i.e., additional deterrence less additional costs of the sanction) exceed those of other sanctions.

[18] *See* Khanna & Dickinson, *supra* note 1.

[19] *See id*.

[20] *See id*. It is plausible that firms agree to a DPA and monitor because that evades liability for certain corporate agents (e.g., the Chief Executive Officer (CEO)). *See* Lichtblau, *supra* note 9. Such an agency cost story is possible, but perhaps unlikely. The reason is that prosecutors often opt for a DPA when the firm provides information on other culpable individuals within the firm.

[21] *See* Khanna & Dickinson, *supra* note 1.

allows them to advise firms more accurately, which is important if the costs of bring "wrong" are high (e.g., the harm caused would be large).[22] Supervisors with frequent on-going contact are then well suited to deter and prevent large harms as well as harms that are difficult to discover.

In light of this, before a monitor is appointed there should be an affirmative determination (after open discussion) by the DoJ or a court about why cash fines are not sufficient for deterrence or why enforcement savings justify the appointment of a monitor as well as why the frequent on-going contact is beneficial. Such a determination serves two functions. First, it helps to ensure that monitors are appointed when they are desirable. Second, it makes it less likely that someone will be able to use a monitor to avoid imposing a cash fine that the firm can pay because if the firm could pay the fine then that would weaken the justification for appointing a monitor.

In addition to discussing when monitors may be desirable, we also need to explore what powers and duties they should have. Monitoring assignments have tended to grant monitors powers over compliance matters, but some assignments seem to have gone quite a bit farther.[23] Generally, there is a relationship between these powers and duties – the greater the power the greater the accountability (e.g., duties or other checks on their power).

I would thus recast the discussion over duties to be one about what kinds of fiduciary duties, if any, should monitors owe to shareholders. Because monitors' decisions may, at times, impact shareholder returns that places them in a position analogous to that of a corporate fiduciary (e.g., a director or top corporate officer). We can use that as our starting point of inquiry.

In the standard fiduciary context (e.g., firms' managers) market forces and fiduciary duties interact to hold the firms' managers accountable, in some measure, for their behavior. For example, if the market for managerial services is competitive, then managers would have little incentive to divert corporate assets or be slack on the job because that may lead to their removal, a denial of a promotion or some other penalty.[24] Similar arguments apply in the context of competitive product markets.[25] However, these market forces have their limits.

---

[22] *See id.*

[23] *See id.*

[24] *See* FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 90–92 (1991).

[25] *See id.*; Khanna & Dickinson, *supra* note 1.

When markets do not register certain slack or where the gains to managers from misbehavior are so great that they are willing to bear the market's negative consequences then the markets have limited ability to constrain managers.[26] In such circumstances, fiduciary duties can provide a helpful disciplining influence.

In contrast, monitors face few market pressures. This is because it is difficult to remove monitors, which in turn weakens the force of any market pressures that might exist.[27] In theory, the monitor's reputation may serve as a constraint, but here too the absence of a developed market for monitor services serves to weaken any reputational penalties a monitor may suffer for poor performance.[28] Indeed, until a more functioning market for monitor services is developed (something I would encourage), one might be inclined to impose some kinds of fiduciary duties on monitors to fill the gaps left by the absence of significant market forces. [29]

This last point suggests that one way in which we can reduce the need for fiduciary duties is by facilitating the development of a market in monitor services. Such a market would, however, be beneficial along other multiple dimensions as well. For example, such a market would enhance competition in the provision of monitor services. In addition, this market could help assuage concerns about the selection and compensation of monitors because the decisions would be more transparent and monitors would face some constraints as well.

How might one facilitate such a market in monitor services? Prior research suggests that we can facilitate such markets by increasing the accountability of monitors to shareholders (or other appointing entity) and by selecting monitors from a pool of qualified individuals (or entities).[30] Information on who is qualified could be housed in some kind of central clearinghouse.[31] Such a market would help enhance the likelihood that monitors were competent, cognizant of their impact on shareholders, and subject to a market for their services, which generates pressures for good performance.[32]

---

[26] *See* EASTERBROOK & FISCHEL, *supra* note 24; Khanna & Dickinson, *supra* note 1.

[27] *See* Khanna & Dickinson, *supra* note 1.

[28] *See id.*

[29] One could provide for the possibility of insurance and indemnification so that monitors do not face crushing liability risks and place limits on shareholders suits to assuage concerns about frivolous suits.

[30] *See* Khanna, *supra* note 1; Khanna & Dickinson, *supra* note 1; Ronald J. Gilson & Reinier H. Kraakman, *Reinventing the Outside Director: An Agenda for Institutional Investors*, STAN. L. REV. 863 (1991).

[31] *See* Gilson & Kraakman, *supra* note 30.

[32] *See* Khanna & Dickinson, *supra* note 1.

Until such a market develops, however, we may need to rely on some version of fiduciary duty. The content of such duties should vary depending on the influence the monitor has at the firm – if the monitor has powers similar to that of a high level executive then their duties should be similar to those on the executive.[33] If the monitor serves in a purely advisory capacity then the duties of an advisor seem more appropriate.[34]

Table 1 summarizes some recommendations for the better functioning of monitors from this analysis that can be used to examine recent reform efforts.

TABLE 1 [35]

DECISION TO MAKE	FACTORS TO CONSIDER
Whether to Appoint a Monitor?	1. Harm caused is large such that cash fines to deter it are considered too large to impose (i.e., the firm's assets are insufficient or the collateral consequences of the fine are too great). 2. The firm's gains from wrongdoing are large and socially unacceptable. 3. There are enforcement savings by opting for a monitor. 4. A supervisor with frequent on-going contact is desirable. ** There should be explicit and open discussion of these issues to ensure that monitors are being appointed when cash fines are no longer a useful option for additional deterrence. This discussion makes it more difficult for someone to appoint a monitor to avoid a higher fine that can be paid. **
How to Appoint a Monitor?	1. The creation of a "market" of sorts for monitor services with the presence of a central clearinghouse. 2. Monitors may owe some duties to shareholders or be subject to increased agency or judicial oversight until the market functions better or until the monitor's sphere of influence at the firm is limited to compliance matters.
Powers of a Monitor?	1. Monitor's powers should vary depending on what is necessary for the task at hand. 2. Greater specificity at the beginning (when negotiating

[33] *See id*.

[34] *See id.*

[35] *See* Khanna, *supra* note 1.

	the DPA) seems desirable especially as it relates to: (a) the scope of the monitor's powers, (b) the reporting chain between the monitor, firm, firm's internal players and government, (c) termination of monitoring assignment upon triggering events (e.g., acquisition), and (d) third party liability. 3. Referral back to appointing agency or court to resolve critical issues that arise.
Duties of a Monitor?	1. The greater the monitor's powers the greater the extent of fiduciary duties or oversight by the appointing agency or the judiciary (especially with the power to remove the monitor).

3. Recent Steps Toward Reform

The concerns surrounding monitors have culminated in the issuance of the Morford Memo and in at least two draft Bills in Congress.[36] These reforms propose to make changes in at least 3 aspects of corporate monitors.

1. Guidelines on when corporate monitors should be appointed and how they should be selected.
2. Judicial oversight of monitoring assignments.
3. Disclosure obligations of monitors.

A. Guidelines on Appointing Corporate Monitors

The Morford Memo 2008 puts forward 3 broad categories of factors to consider in appointing monitors.[37] First, monitors should be appointed only if their benefits exceed their costs (including their impact on the firm's business operations).[38] Second, the monitor's primary mandate should be to enhance

[36] Another important reform was the Filip Memo which clarifies that waiver of attorney-client privilege by the firm is not a prerequisite to obtaining a DPA. *See* U.S. DEPARTMENT OF JUSTICE MEMORANDUM ON PRINCIPLES OF FEDERAL PROSECUTION OF BUSINESS ORGANIZATIONS, [*hereinafter* Filip Memo], August 28, 2008.

[37] *See* U.S. Department of Justice Memorandum on Selection and Use of Monitors in Deferred Prosecution Agreements and Non-Prosecution Agreements with Corporations [*hereinafter* Morford Memo], March 7, 2008. Available at: http://www.usdoj.gov/dag/morford-useofmonitorsmemo-03072008.pdf.

[38] *See* Morford Memo, *supra* note 37.

current and future compliance.[39] Finally, the Memo lists 9 more specific factors (provided below), which should be applied flexibly given the variety of cases before the DoJ.

1. Before selecting a monitor the firm and government should discuss the monitor's qualifications, avoid conflicts of interest and select someone on the basis of merits only. To avoid conflicts the DoJ will set up *ad hoc* committees to consider candidates. The Office of the Deputy Attorney must approve the selection and the monitor must be impartial.
2. A monitor is not an agent for either the firm or the government.
3. A monitor should focus on assessing and monitoring a firm's compliance with the DPA as it relates to reducing future wrongdoing (i.e., its compliance programs).
4. The monitor's obligations should be no more than necessary to reduce the risk of future offending.
5. In some situations it may be desirable to have the monitor make periodic reports to both the government and the firm.
6. If a firm declines to follow a monitor's recommendations then it should provide reasons for that choice, which the Government can rely on to decide whether the firm has met its obligations under the DPA.
7. The DPA should identify "any types of previously undisclosed or new misconduct that the monitor will be required to report directly to the Government".[40] The monitor should have discretion as to what to report to the Government.
8. The duration of the DPA should be targeted to the concerns that exist at the firm and to remedial measures being taken.
9. Finally, the DPA "should provide for an extension of the monitor provision(s) at the discretion of the Government in the event that the corporation has not successfully satisfied its obligations under the agreement. Conversely, in most cases, an agreement should provide for early termination if the corporation can demonstrate to the Government that there exists a change in circumstances sufficient to eliminate the need for a monitor." [41]

[39] *See id*.
[40] *See id*.
[41] *Id.*

In addition to the Morford Memo, two House Bills add further details to the process of monitor selection.[42] In particular, they require the selection of monitors to occur from a public national pool of pre-qualified candidates and that the final selections receive judicial approval.[43] Further, and in contrast to the Morford Memo, the House Bills require monitors to have "experience in criminal and civil litigation"[44] rather than being individuals with compliance expertise (even if they are not attorneys).[45] The House Bills also envisage an open and competitive selection process where, like the Morford Memo, monitor's powers are limited to compliance concerns thereby reducing the need for fiduciary duties. Finally, the House Bills also impose some structure on the compensation of monitors by requiring that it be based on a pre-determined fee table.[46] This stands in contrast to the Morford Memo's silence on this issue.

Taken together the Morford Memo and the House Bills appear consistent with measures to facilitate a market for monitor services and are broadly consistent with the analysis presented earlier with respect to when monitors are desirable. There are, however, important differences as well.

First, the Morford Memo emphasizes the importance of comparing the costs and benefits of monitors before appointing them and includes in the measure of costs the impact on the firm's business. This seems a good proxy for the costs associated with supervisor-type sanctions (e.g., disruption to firm business) discussed earlier and appears to be a positive development.[47] However, there is no discussion of whether a cash fine might obtain the desired level of deterrence thereby avoiding the need for a monitor. A useful reform would then be to have the DoJ or other enforcement authority state why they think a cash fine would be insufficient. This will aid clarity in decision making as well as reducing concerns that monitors are being appointed to avoid a higher cash fine because if that were true (i.e., there was a higher cash fine the firm could pay) then the above analysis suggests that the monitor sanction would not be used.

---

[42] *See* ACCOUNTABILITY IN DEFERRED PROSECUTION ACT OF 2008, H.R. 6492, 110TH CONGRESS, 2D SESSION (July 15, 2008), available at: http://www.govtrack.us/congress/billtext.xpd?bill=h110-6492; ACCOUNTABILITY IN DEFERRED PROSECUTION ACT OF 2009, H.R. 1947, 111TH CONGRESS, 1ST SESSION (APRIL 2, 2009), available at: http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:h1947ih.txt.pdf

[43] *See* H.R. Bill 6492 (and HR 1947), *supra* note 42.

[44] *See id*.

[45] *See* Morford Memo, *supra* note 37.

[46] *See* H.R. Bill 6492 (and HR 1947), *supra* note 42.

[47] The Morford Memo suggests a monitor is unnecessary when a firm sells off an offending division. This suggests that non-compliance can be isolated to the division that was sold off. This is a questionable assumption for firms where managers move between divisions or where members of top management may use a particular division to engage in illegal acts (corruption raises such concerns).

Second, the House Bills envisage a process where the monitor is selected from a national pool of qualified candidates with final approval by the court. This seems broadly consistent with the suggestion to have a central clearinghouse with information on likely monitors. Further, the House Bills require monitors to have substantial litigation experience (civil or criminal). Although this helps broaden the pool of monitors from former government officials to other attorneys with litigation experience, it may still be a bit too narrow. The reason is that compliance work is only partly about litigation experience, it also often involves understanding how firms operate and how items are produced at a firm (e.g., products or financial statements) which may be expertise more often seen with non-attorneys (e.g., forensic accountants, product specialists). In this respect, qualifications indicating expertise in compliance or risk management may be more desirable. The Morford Memo also assists in facilitating a market for monitor services by discussing the notion of removing the monitor which may enhance market pressures on the monitor.

Third, the Morford Memo encourages the government and the firm to discuss in detail the scope of the monitoring assignment and attempts to narrow it to compliance efforts (rather than broader firm activities). This helps to reduce the need for fiduciary duties on monitors. In addition, the call to have firms actively involved in the process of appointing the monitor (and setting up ad hoc Committees at the DoJ) helps to make monitors not only more accountable to firms, but also more independent from the DoJ.

Fourth, the House Bills also require that monitors receive payments based on a flat and fixed fee structure.[48] Although such a step helps to constrain excessive compensation, it does so at the risk of hampering the development of a market for monitor services. The key concern with a flat fee is that it treats each expert's time as if it were fungible. This is generally not true. For example, the skills required to be a compliance expert on issue X may be different (and more expensive to obtain) than the skills to be a compliance expert on Y. Flattening out the differences may hurt the development of a market for monitor services especially for expertise requiring greater time and investment to develop.

Nonetheless, avoiding a flat fee does not mean we have no ways to limit excessive compensation. One option may be to require open competitive bidding for monitoring assignments. Alternatively, we could envisage judicial

[48] *See* H.R. Bill 6492 (and HR 1947), *supra* note 42.

review for fees above a certain amount (e.g., $2000 per hour) where the monitor and firm bear the burden of proving why this rate is appropriate. We could even consider having multiple flat fees (one flat fee for all experts in X and another for experts in Y). Although no option is perfect, they do allow some oversight on compensation while allowing for the development of a market.

B. What Role Should the Judiciary Play in the Monitoring Process?

The House Bills seem to indicate a preference for judicial oversight of the monitoring process (something the Morford Memo does not discuss in depth).[49] Judicial oversight can be useful, but it may be a matter of timing and degree. For example, requiring judicial approval before finalizing a DPA and monitoring assignment (e.g., on monitor compensation) may avoid many problems at fairly little additional cost, as the issues will be fresh in the memories of prosecutors and firms. However, once the monitoring assignment is underway judicial oversight may be more costly because the parties (and the court) would need to gather further information and get "up to speed" all over again. Moreover, frequent judicial oversight over the course of the monitoring assignment could undermine one of the benefits of monitors – economizing on enforcement resources. One way to address these concerns might be to have well drafted DPAs and monitoring assignments and judicial oversight triggered by certain limited events (e.g., an acquisition, repeated instances of wrongdoing) so that the costs of the review arise only in some instances.

C. Should the Reports of Monitors Be Made Available to the Public?

Finally, should the monitor's reports be made public? After all, a criminal prosecution (a matter of public interest) was averted through the DPA and it seems that the public has an interest in knowing what the monitor found.

The House Bills presume that monitors' reports will be available, at least to the court, but are silent on public disclosure.[50] The Morford Memo expects monitors to disclose evidence of credible wrongdoing to the Government, but says little about public disclosure.[51] Generally, disclosure of the monitors' reports is preferable because it provides information about firm wrongdoing (thereby informing victims and potentially helping to reduce the severity of the

---

[49] *See id.*

[50] *See* H.R. Bill 6492 (and HR 1947), *supra* note 42.

[51] *See* Morford Memo, *supra* note 37.

harm) and also about ways to reduce this kind of wrongdoing. However, some parts of the reports may not be essential to enhance the chances of reducing wrongdoing or informing victims, but rather may be more embarrassing to the firm or undermine its competitive position. Such situations may call for some power (either with the court or the DoJ) to redact parts of the monitors' reports.[52]

From this discussion it appears that substantial steps have been taken via the Morford Memo and the House Bills to facilitate the development of a market for monitor services. Further steps as discussed above may also be warranted to enhance the development of this market which helps to enhance the functioning of monitors as well as add transparency to the process of their appointment.

Overall, my analysis suggests that in addition to the Morford Memo and the House Bills the following steps may prove particularly advantageous.

1. Explicit discussion by the DoJ about why a cash fine would not suffice for deterrence and why a monitor with frequent on-going contact with the firm would be desirable.
2. Some oversight on monitor compensation is desirable, but a pure flat fee should be adopted very cautiously. Instead, judicial review (triggered by fees crossing some specified threshold), open competitive bidding, or multiple flat fees may be a good balance between encouraging development of compliance expertise and reducing excessive compensation concerns.
3. The groups of people who are qualified to act as monitors should be expanded to include not only former enforcement officials, but also attorneys with substantial litigation and others who have experience in compliance matters.
4. Arranging for some judicial oversight before a DPA and monitoring assignment are finalized may be desirable. However, on-going oversight may be quite costly and should be limited to only certain triggering events (e.g., acquisition of the firm).
5. Public disclosure of monitor's reports should be the norm subject to the power of the court or the DoJ to redact certain information.

Finally, further study on how to encourage the development of a market for monitors would be useful. Indeed, one may be able to learn more about how

[52] Of course, firms should not be permitted to take public positions that are inconsistent with the monitor's reports without clear explanation.

to facilitate this market by examining the development of other affiliated markets. Such markets might include the market for Independent Private Sector Inspector Generals in the New York area and the general market for independent directors.[53] Further, the development of a market for monitor services may have important consequences for corporate governance. If we think of boards as serving two functions – strategic advisors and watchdogs – then the presence of monitors may reduce the need for the board to act as a watchdog. This may be a beneficial development because the board's two roles operate in some tension with each other and a monitor may be better suited to the watchdog role. [54] Thus, the development of a market for monitors may help to clarify and simplify the role of the board and thereby enhancing its functioning as well.

4. Concluding Remarks

The growth of corporate monitors as an institution for enhancing compliance has been rapid. However, in the last year or so, the rather unregulated growth of corporate monitors has come in for criticism from many corners. In this statement I examine the structure of corporate monitoring assignments and explore how the use of the monitor can be improved. My analysis suggests that many of the recent developments (e.g., the Morford Memo and House Bills) are steps in the right direction to facilitate the growth of a market for monitor services and to enhance the impartiality and transparency of this new enforcement tool in the fight against white collar crime. However, some further steps may be useful as the market for monitor services begin to develop. In particular, requiring explicit discussion of why other sanctions are not sufficient for deterrence and why monitors are beneficial seems important as does opening up the market for monitor services to more groups of experts. Further, restrictions on compensation should be considered cautiously to avoid impeding the growth of the market, but oversight with disclosure may prove to be a beneficial approach. Moreover, the impact of the development of this market on compliance and corporate governance is an area rich for further inquiry. In particular, how the development of a market for monitor services may help to clarify and simplify the role of corporate boards and our expectations of them could in the long run prove to be a valuable development.

---

[53] *See* Ronald Goldstock & James B. Jacobs, *Monitors and IPSIGS: Emergence of A New Criminal Justice Role*, 43 CRIMINAL LAW BULLETIN 217 (2007).

[54] Monitors who have substantial compliance expertise and frequent on-going contact with the firm are better placed to be watchdogs for wrongdoing than the board which may not have that level of compliance expertise and who meet only a dozen or less times a year.