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DPA corporate monitorships in the UK

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Jo Rickards and Johanna Walsh at Kingsley Napley in London look at what to expect from corporate monitorships included as part of a deferred prosecution agreement – and how to get the most out of them.

Although monitors have been used regularly in the US over the past few decades, with a marked increase in their use post-Enron, they have not been used with the same frequency in the UK. With the introduction in February 2014 of deferred prosecution agreements (DPAs), this is set to change. Monitors are independent third parties, usually law firms, risk consultancies or professional services firms, appointed to oversee and report on a company's internal controls and compliance functions following a criminal or regulatory investigation.

Monitorships are not new to corporate criminal investigations in England and Wales. In 2008, when the Serious Fraud Office (SFO) obtained a civil recovery order against Balfour Beatty for payment irregularities in connection with the construction of an Egyptian library, part of that order included "a form of external monitoring for an agreed period". The following year, after Mabey & Johnson's plea to foreign bribery and breaching UN sanctions, the company had to instruct an SFO-approved monitor for up to three years. This was described by Judge Geoffrey Rivlin as an expensive exercise, with the cost of the monitor for the first year capped at £250,000.

The resolution of the Innospec corruption investigation in 2010 saw the first US-UK joint monitorship. The circumstances of the case meant that Lord Justice Thomas allowed the three-year monitoring arrangement, which had been agreed prior to sentencing in the US and UK, but in doing so expressed his general disapproval of it. He likened the monitorship to an expensive form of probation order and deemed it unnecessary for a company with new management whose auditors were aware of the past conduct and whose directors were aware of the penal consequences of similar future conduct. The judge concluded that in future the proposed appointment of monitors would need to be fully explained to the court in terms of cost effectiveness as money would be better spent on compensation, confiscation or fines.

Although monitors were included in both of the civil recovery orders agreed between the SFO and Macmillan Publishers (in 2011) and Oxford Publishing (in 2012), the issue of monitorships has not been considered by a criminal court since Innospec.

That is set to change. Monitorships are not a compulsory feature of a DPA and will only be imposed where companies do not already have effective corporate compliance programmes in place. However, the attention given to monitoring programmes in the DPA Code of Practice is a good indication of the importance that prosecu-

tors place on them as a means of reducing the risk of corporate recidivism. The code sets out a framework for the appointment of monitors including that companies will be responsible for all of the costs of the monitorship (including the prosecutor's costs) and must give the monitor complete access to all relevant aspects of its business. The code suggests that prior to the approval of the DPA, the prosecutor and the company should agree between them which monitor will be appointed, the cost and terms of the monitorship and the scope of the first year work plan.

There may also be an uptake in the use of monitors outside the DPA setting. The Public Contracts Regulations 2015, in force in England since February 2015, allows companies who are debarred from bidding for public work to recover their eligibility for such work by demonstrating that they have "self-cleaned". One of the steps is through the introduction of measures to avoid future criminal offences. Companies could instruct monitors to demonstrate their commitment to this course, using the report in the bidding process as evidence of their remediation.

Companies should not view monitors as a soft option or think that engaging a monitor to reduce the overall financial penalty will be cost effective. Monitorships can be very expensive and intrusive. In the US, following its conviction in 2013 for conspiring to fix the prices of its e-books, Apple objected unsuccessfully to the imposition of a corporate monitor, on the grounds that it would be expensive, burdensome and would have few benefits. Following the appointment of the monitor, Apple became entangled in a series of disputes with him and applied, again unsuccessfully, for his disqualification.

Going head to head with a monitor is expensive and time consuming and rarely ends well. Whether a monitor is necessary under a DPA or to avoid the imposition of one later or to demonstrate self-cleaning, there are a number of issues that a company should consider to get the most out of the relationship.

Understand the relationship with the monitor

The email correspondence disclosed in the litigation between Apple and its monitor is illustrative of a company failing to understand its monitor's role. At the start of the relationship, Apple said that the monitor "like all of Apple's legal service providers" must abide by the company's policies on fees and expenses. The monitor reminded Apple of his firm's independence and the circumstances of his appointment, making clear that he was "not [acting] as counsel to Apple subject to its direction and control".

Many of the monitors appointed in the US and here have been lawyers. Although the company is responsible for payment of the monitor's fees, the relationship is not like a lawyer-client relationship. A monitor is an independent third party, usually appointed to fulfil a court-approved function. The monitor's primary duty is to that role and the monitor does not owe a duty, in the conventional lawyer-client sense, to the company or its shareholders.

Such issues will be avoided under the code which sets out that the monitor's costs, terms of reference and reporting requirements will all be negotiated and agreed prior to the DPA being approved by the court.

Choose your monitor carefully

A company should play an active role in identifying its monitor. The code envisages a process whereby a company will indicate its preferred choice of three monitors which the prosecutor should approve unless there is a good reason not to do so.

Companies who are the subject of a criminal investigation should also consider appointing a monitor before they even enter into DPA negotiations (assuming they are invited to) or are prosecuted. Appointing a monitor early to advise on and oversee a revamped and effective corporate compliance programme is a good way to demonstrate that a company is serious about, and has taken genuine steps towards, remediation. This can influence whether the prosecutor will invite the company to enter into DPA negotiations and even whether it is in the public interest to prosecute the company. It is also likely to mean that if a DPA is agreed, a prosecutor will be less inclined to impose a new monitor.

Companies should bear in mind the advantage of appointing a monitor with local knowledge and understanding of what can and cannot be done in the context of the applicable laws. This is particularly important for companies with global operations. Local and sectoral expertise is also important as it will mean the monitor grasps the issues quickly and may also mean a more respectful relationship with those in the company, leading to less friction in the company's day-to-day dealings with the monitor.

Scope the monitorship fully

The code recognises that the varying facts of each case and the nature and size of the company mean that no two monitoring programmes will be the same. Companies must ensure that the terms of reference and work plans are tailored sufficiently to the needs of their business and take into account the company's risk profile, size and geographic reach.

The US has seen so-called "runaway monitors", who are given such broad or ill-defined scope that they incur fees without actually benefiting the company. An example is a former judge appointed as a monitor as part of DPA agreed with a university in the US in respect of a fraud. The monitor was mandated to investigate any alleged wrongdoing at his discretion and require the university to take any steps necessary to comply with the DPA and applicable laws. During the monitorship, he filed reports alleging misconduct by employees – leading to termination of their employment – and also employed law firms and auditors to assist him. After six months in post his bill ran into millions and exceeded the value of the original fraud. Proper scoping at the outset will prevent this from happening, allowing for a forensic assessment of what is required in the particular company's case and setting expectations from the start.

Companies should ensure that regular update meetings with the monitor are built into work plans to allow for feedback and ensure that the company can implement any interim suggestions before the monitor reports to the court. The company should also ensure that it has the time and opportunity to review and comment on the draft reports before they are finalised. This will mean the company can ensure that recommendations are feasible and that they have the opportunity to correct any factual misunderstandings that may have arisen.

Minimise the length of the monitorship where possible

The length of the monitorship is another factor that companies should consider: the longer the monitoring period, the higher the bill. Monitors will add the most value in the first year or two of the relationship. The code provides for the inclusion of an escape clause whereby provision will be made for the termination or suspension of the monitoring programme if the monitor and prosecutor are satisfied that the company's policies are functioning properly. An escape clause is a good way to incentivise companies that might not otherwise embrace the appointment of a monitor. It should be noted that the code also provides for the converse scenario, whereby the length of the monitoring period can be extended (provided it is not longer than the length of the DPA itself) if the company has not satisfied its obligations under the mandate.

An alternative model which has developed in the US is the "hybrid monitorship" where a monitor is appointed for a specified period (usually 18 months of a three-year period) after which the company can move to a programme of self-reporting and self-monitoring for the remaining period of the DPA. This will not only reduce – often halve – the cost of the monitor, but has the additional benefit of shortening the period of intrusion in which a third party has complete access to all relevant aspects of the company's business.

Ensure internal engagement

One of the best ways for companies to make the most of having a monitor is to engage the relevant functions – internal audit, compliance, legal and finance – in the process from the outset. These control functions will be responsible for implementing the monitor's suggestions and continuing the monitor's legacy after the monitoring programme has come to an end. If these functions do not take the monitor's suggestions forward and encourage cultural change then the monitor's legacy will be lost.

Conclusion

Monitors are going to be part of the mix of sanctions and remediation in sentencing for UK companies in the coming years. Although there haven't been any DPAs agreed here yet, the director of the SFO has publicly stated that he expects at least two DPAs to be completed by the end of 2015. Whether these will require monitors remains to be seen and, if they do, they will have to get over the judicial hurdle when it comes to approving the terms of the DPA given Lord Justice Thomas's view about their necessity for remediated companies.

In the meantime, companies can prepare for monitorships by drawing lessons from the US. The key challenges for a company faced with a monitor are to choose wisely, try to minimise the cost and disruption to the business while ensuring that the company makes the most of having the monitor and implements any suggestions to strengthen corporate governance and avoid the prospect of being investigated or prosecuted again.

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