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## **Key Issues in Internal Investigations**

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## INTRODUCTION

Virtually every major public corporation has conducted at least one significant internal investigation in the past few years. The reasons for this development are many, including the post-Sarbanes-Oxley environment and the policies of the Department of Justice, the Securities and Exchange Commission and other law enforcement agencies that state that credit may be given for conducting internal investigations. While high profile internal investigations have occurred in every major corporate scandal, such as WorldCom, Enron, Adelphia and Tyco, they have also been employed in far more discrete and less significant matters.

Every internal investigation will have unique issues, circumstances, dimensions, challenges and outcomes. While an internal investigation can provide great benefits to a corporation and its senior executives and directors, it can cause serious harm if it is not conducted properly. This paper identifies and discusses many of the key issues that arise in internal investigations. Because each investigation is different, the responses to these issues may change depending on the individual circumstances. Further, this list is not all inclusive and there are many additional issues that will need to be addressed in each investigation.

### **I. When should an internal investigation be conducted?**

Determining whether to conduct an internal investigation should be considered carefully. Once the decision is made to conduct an investigation, it typically must be completed. If an investigation is halted before it is completed, it can lead to claims of a cover-up or failure to ascertain the facts.



Internal investigations typically should be conducted when there have been credible allegations or suspicions of significant wrongdoing, misconduct or ethical lapses. There are many factors that are important in determining whether an internal investigation should be conducted, including the magnitude of the alleged harm, the existence of any governmental inquiry, the number of employees involved, the duration of the alleged wrongdoing, the prior disciplinary history of the company, the culture of the company and the aggressiveness of the Board. Internal investigations may also be appropriate even if there have not been specific allegations against a company, but there have been allegations of misconduct within the industry or against a competitor. A current example is whether a public corporation has any issues related to the backdating of stock option grants. It is not uncommon for problems at one company to be present at a similarly situated company.

## **II. Who should conduct the internal investigation?**

Internal investigations need to be credible and are typically most effective if they are perceived as being truly independent from the company. Thus, they are typically done by an outside law firm which has not done extensive work for the company. An outside law firm that has experience in conducting internal investigations likely can conduct them more effectively and efficiently. While there are significant benefits to having an outside law firm that has not done much prior work for the company conduct the investigation, it may result in higher costs since the law firm will have a greater learning curve with respect to the structure, business and culture of the company. If specialized expertise is needed, the outside law firm may need to retain experts, such as accountants, trading specialists or forensic investigators.



If a governmental investigation is already underway, it may be problematic for the law firm representing the company in that investigation to also conduct the internal investigation. Given that the goals of representing a company in a governmental investigation and conducting an internal investigation are not entirely consistent, questions may be raised whether the law firm defending the company can be properly objective in conducting the internal investigation. If the allegations are significant, it is likely more effective not to have a law firm perform both roles.

### **III. Who should control the investigation?**

Internal investigations are typically controlled by the Board of Directors, the Audit Committee of the Board or a specially created Committee of the Board. If there have been any allegations or suggestion that a Chief Executive Officer, General Counsel or member of the Board engaged in wrongdoing, those persons should not have any involvement in, or influence over, the investigation. An engagement letter should detail the identity of the client, the scope of the investigation and establish the appropriate privileges.

### **IV. Should in-house counsel be involved in conducting the internal investigation?**

To maintain the independence and integrity of the process, it is usually better for in-house counsel not to be involved in conducting the investigation. However, it is typically appropriate and beneficial for the company to designate an employee to act as a “facilitator” for the law firm conducting the investigation to identify sources for relevant documents and to assist in arranging interviews, and performing other administrative tasks. This “facilitator” does not necessarily



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have to be a member of the legal department, and should not otherwise participate in the investigation or be privy to the findings.

**V. How should an internal investigation be organized and initiated?**

While every internal investigation is organized differently, there are certain characteristics that are common to each. First, careful attention should be given to putting together the correct team of lawyers and any necessary experts. Since an important objective of an internal investigation is to ascertain the facts in an objective manner and not advocate a position, it is important to have lawyers who understand this role. Second, a lead lawyer should be designated to coordinate and supervise the investigation, and serve as the primary editor of any written report. If the investigation covers a number of different issues, it may be beneficial to create issue teams and to have a leader for each team. Third, a workplan should be prepared and revised as necessary so that the team clearly understands the issues to be investigated and the responsibilities of each team member. Fourth, there should be frequent communications among the team as it is important that everyone be aware of developing issues and facts. If it is a large investigation involving a number of lawyers, weekly or more frequent status reports are important. Fifth, the confidentiality of the work product should be maintained. Any premature leaks of information will make it harder to get candid responses during interviews and will challenge the integrity of the process and any privilege claim. Sixth, efforts should be made to minimize the disruption to the ongoing business. While internal investigations are certainly important and should be conducted expeditiously, they can cause harm if they create anxiety among employees or cause other damage to the company.



## **VI. How should privileges be maintained?**

Preserving the attorney-client and attorney work product privileges may be one of the toughest challenges in conducting an internal investigation, particularly if the decision has been made at the outset to release publicly a written report. Given the complexity of this issue, it is not possible to analyze fully in this paper the numerous factors that must be considered. As a general rule, if information is not maintained in a confidential manner, then it will make it more difficult to maintain any privilege. For example, if a written report is to be publicly released, it will be difficult to maintain the attorney-client privilege.

At a minimum, the engagement letter should make clear that a purpose of the investigation is to give legal advice. In addition, steps should be taken to limit the number of people with access to the process and information as the investigation is ongoing. Moreover, all documents prepared should contain a “privileged and confidential” legend.

## **VII. Should notice of the internal investigation be given to employees?**

With certain exceptions, a notice of the internal investigation generally should be provided to all employees so that they understand the purpose and nature of the investigation. Otherwise, inaccurate and damaging rumors may permeate the company. Employees should be told that the investigation is confidential and that they should not discuss the investigation or the underlying issues with anyone.



### **VIII. How should documents and other information be preserved?**

A request to preserve documents should be distributed promptly to all employees who may have relevant information. The notice should provide sufficient detail as to the scope of the internal investigation, but should not telegraph the direction of the investigation or otherwise jeopardize its integrity. In addition to distributing the document preservation notice, any corporate document destruction policies related to potentially relevant documents should be suspended. Further, relevant e-mails should be gathered from the computer network and in some situations, the hard drives of relevant personnel should be gathered promptly. Moreover, if there is a concern about the destruction of documents, the office and files of impacted employees should be secured.

### **IX. How important are e-mails?**

E-mails are a critical source of information given that they reflect the contemporaneous and sometimes unfiltered state of mind of the sender. Great efforts should be taken to gather e-mails and restore any that have been deleted. E-mails should typically be reviewed and analyzed for each witness who is interviewed. To facilitate the review, it may be beneficial to conduct key word searches to identify the most relevant e-mails.



**X. When and how should interviews be conducted?**

Interviews are typically the most valuable source of information in an internal investigation. It may be advantageous to conduct initial interviews at the outset of the investigation to obtain a witness' version of events before it may be influenced by other factors and to get a narrative overview of relevant events. These interviews may be conducted before documents are gathered and analyzed. If such preliminary interviews are conducted, it may be necessary to interview the most relevant people on more than one occasion after documents are reviewed and interviews of all of the less significant witnesses have been conducted.

Care should be taken not to be adversarial in interviews. If interviews become contentious, it can cause an allegation of lack of objectivity and weaken the credibility of the findings. The goal in interviews should be to obtain as much information as possible and then test its accuracy against documents, other testimony and any additional information obtained. In addition, a questioner should be careful not to disclose what other witnesses may have said or telegraph the direction of the investigation.

**XI. Should interviews be recorded?**

If a verbatim record of an interview is needed, then the interview should be recorded. A verbatim record may be required if it is determined at the outset to provide the government with the record of all interviews. Absent this requirement, it is generally better not to record the interviews as a court reporter may inhibit or chill a witness. In such situations, detailed notes of



the interview should be taken so that there is a comprehensive and accurate record of the interview.

**XII. Can an employee have a lawyer present at the interview?**

An employee generally should be allowed to have a lawyer present at an interview if requested. However, there is no right to a lawyer and this accommodation should not be used to delay significantly the timing of the interview. Moreover, the lawyer for the witness should not interfere with the questioning at the interview. To ensure that the record is complete as possible, the lawyer for the witness may be given an opportunity to ask questions of the witness at the end of the interview. Given that the goal of an internal investigation is to gather the facts in as thorough and accurate a manner as possible, this additional questioning could add important information to the record.

**XIII. Should a company pay for a lawyer for an employee?**

Whether the company indemnifies the cost of a lawyer typically depends on the past practices at the company, the by-laws, the seniority of the employee, the rights to indemnity and the types of allegations being investigated. In most cases involving senior officers, the company should pay for a lawyer. It should be noted, however, that government regulators have requested in the past that certain companies not indemnify employees who were targets or subjects of investigations. In one challenge to this tactic, a U.S. District Court found that such request was unconstitutional.



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**XIV. Should employees be offered the opportunity to submit a “white paper” or similar materials?**

It is critical that the findings of any internal investigation be accurate and thorough. Thus, it may be beneficial to the process to obtain information from different perspectives. One way to promote this objective is to give relevant employees the opportunity to submit information that they believe is relevant. This could include asking an employee to submit a “white paper” to respond to a particular issue or question.

**XV. Should a written report be prepared?**

Whether or not a written report should be prepared can be one of the more difficult questions to resolve in any internal investigation. Written reports generally add credibility to an internal investigation. Moreover, if a goal of the investigation is to show cooperation with the government, then a written report is likely required. However, unless there is a clear reason at the outset to prepare a written report, it may make sense to defer that decision until the investigation is completed and the outcome and consequences of the investigation are better understood.

There are substantial reasons not to prepare a written report given the risks involved. Additional damage to a company could occur if the findings are far worse than thought at the outset of the investigation. In addition, the investigation could uncover additional wrongdoing that may have to be disclosed in a written report. Moreover, applicable privileges may be waived if a written report is released to third parties.



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**XVI. Should the company or employees be allowed to review the report before it is finalized?**

Typically, a written report should not be reviewed by anyone before it is finalized to preserve its integrity and independence. However, in certain situations, especially when the issues are of a highly technical nature, it may be beneficial to let someone who is not implicated by the internal investigation review the factual portion of a near-finalized draft to ensure the accuracy of the report. The primary objectives of having an accurate and thorough report will sometimes outweigh the potential harm to the integrity of the process by having someone review the report before it is finalized.