

# ***The Worst Day Of A CEO's Corporate Life***

**Jerome Gabig**  
*Huntsville Attorney*

(256) 509-0279

[Gabig3@comcast.net](mailto:Gabig3@comcast.net)

# A CEO's Day Of Infamy

- An “Inter-Agency” Task Force of CID, AFOSI, DODIG, and NASA IG is in the lobby.
- They have a search warrant and plan to confiscate every hard drive in the company
- They have asked for your cooperation to interview employees
- The local newspaper and TV station have reporters on the scene
- You are only topically aware of the alleged wrongdoing

**United States Attorney Alice H. Martin**

**Northern District of Alabama**

FOR IMMEDIATE RELEASE CONTACT: Jill Ellis

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[www.usdoj.gov/usao/aln](http://www.usdoj.gov/usao/aln) FAX: ( 205) 244-2171

**ALABAMA DEFENSE CONTRACTOR AND ITS OWNER INDICTED**

**FOR ILLEGAL EXPORT OF MILITARY DEFENSE ARTICLES**

**BIRMINGHAM, AL** - An Alabama company and its owner have been indicted by a Federal Grand Jury on charges of illegally exporting military defense technology without a license, fraud involving aircraft parts, and submitting false documents. The five-count indictment charges AXION CORPORATION and its owner ALEXANDER NOOREDIN LATIFI, 59, both of Huntsville, Alabama, and is announced today by Kenneth L. Wainstein, Assistant Attorney General for National Security, and Alice H. Martin, United States Attorney for the Northern District of Alabama.

Welcome  
To Mr.  
Latifi's  
World

# A CEO's Day Of Infamy

## The Three Most Likely Causes

- Disgruntled employees
- Employee bad judgment
- Ignorance

# Disgruntled Employee Example #1

- Axion business model
- Fired embezzling bookkeeper
- Bookkeeper “downloads” to DODIG
- Many years of Special Agent time devoted to investigating
- Axion suspended
- Axion acquitted
- Business essentially ruined

# Disgruntled Employee Example #2

- Successful Huntsville 8(a) Company
- Largest contract was a subcontract with a top five government contractor
- Disgruntled employee claimed 8(a) had submitted false claims
- 8(a) retained a retired SES attorney to conduct investigation
- Because of excellent “damage control,” no adverse impact



*If It Can Happen To Boeing....*

# Bad Judgment Example #1

- Boeing possessed a large amount of rival LM proprietary data during the 1998 Evolved Expendable Launch Vehicle (EELV) competition
- The data was capable of providing great insight into LM cost and pricing
- Boeing waited four years to disclose the misconduct

*If It Can Happen To Boeing....*

# Bad Judgment Example #1

- In July 2003, the Air Force suspended three of Boeing's Integrated Defense System business units.



*If It Can Happen To Boeing....*

## Bad Judgment Example #2

- In 2002, Boeing's CFO offered a job to Darleen Druyun, the Air Force chief acquisition official.
- For a reduced sentence, Druyun admitted that she favored Boeing on multiple contracts because of favors granted by Boeing.

*If It Can Happen To Boeing....*

## Bad Judgment Example #2

- Boeing's CEO was forced to resign
- Contracts awarded to Boeing by Druyun were successfully protested
- Boeing's recent loss of the Air Force tanker program is largely attributable to the scandal

*If It Can Happen To Boeing....*

## Bad Judgment

In June 2006, Boeing  
settled Example #1 and  
Example #2 collectively  
for \$615 million

*If It Can Happen To Boeing....*

# Bad Judgment = Bad Ethics

“I also went back and counted the number of vice presidents who have been separated from the company for ethics violations over the last few years. The total is 15.”

Boeing General Counsel (2006)

*Local*

# Bad Judgment Example #3

- Successful Huntsville large business
- Hires a “hard charging” retired military officer to pursue \$2X,000,000 contract
- Selected for award
- Disqualified because employee repeated contacted SSA and SSAC members
- Because of excellent “damage control,” no other adverse action against company

# Ignorance Example #1

- Georgia company makes small arms training simulators
- Imports demilitarized small arms from Europe to insert laser beam firing
- Ignorant that ITAR applies
- Federal agents seize all records and most of inventory
- Delinquent on delivering products to clients
- Impact almost fatal to company



# Ignorance Example #2

- In 1995, Coast Janitorial Service was awarded a contract at Redstone Arsenal for \$19,128,277
- Coast's Project Manager, "to keep overhead low," did not pay employees who worked overtime time and a half



# Ignorance Example #2

- Instead, Coast credited employee with “comp time” which was paid at regular hourly rates.
- DOL found SCA violation involving two employees at an amount of \$6,596.

# Ignorance Example #2

- Coastal responsible for “willful and deliberate” violations of supervisor
- Coast debarred for 3 years
- President, Mr. Grimes, debarred
- VP, Mr. Scott, debarred

## *Back To Mr. Latifi's World...*

**The decisions you make on Day #1 could be the most important decisions you make during the crisis.**

# A CEO's Day Of Infamy

## Range of First Day Decisions

- No Comment v. Press Release
- Denial v. Admissions
- Commit to full cooperation v. Do not cooperate
- Call an “All-Hands” meeting
- Offer to pay legal fees for any employee whom Government wishes to interview

# A CEO's Day Of Infamy

## Consequences Of 1<sup>st</sup> Day Decisions

- **No comment.** *Lack of damage control on adverse publicity*
- **Denial.** *Debarment Official annoyed*
- **Admission.** *Used against company in civil and criminal proceeding*
- **Commit to full cooperation.** *Damaging evidence used against company*

# A CEO's Day Of Infamy

## Consequences Of 1<sup>st</sup> Day Decisions

- **Don't cooperate.** *Greater chance of suspension & debarment*
- **Call an "all-hands" meeting.** *Risk of accused of obstruction of justice*
- **Do not call meeting.** *Employees bewildered; loss of morale*
- **Offer to pay employee's attorney fees.** *Expensive; annoys Government*
- **Do not offer.** *Appear disloyal to employees*

# Guidance For A Prudent CEO

## I. Precautions

## II. Preparation

## III. Reaction



# I. Prevent

**The best  
precaution is an  
exceptional  
compliance  
program**

## *II. Prevention*

# Compliance Program

- Prevent and detect improper conduct
- Promote an organizational culture that encourages the highest degree of honesty and integrity, ethical conduct, and a commitment to compliance with the law

## *II. Prevention*

# Compliance Program

- Facilitate timely discovery and disclosure of improper conduct.
- Ensures corrective measures are promptly instituted
- Tailored to the size of the organization and its involvement in government contracts

## *II. Prevention*

# Compliance Program

## New FAR § 52.203-13

Within 30 days of contract award the Contractor shall:

- o Have a written code of business ethics and conduct; and
- o Provide a copy of the code to each employee engaged in performance of the contract

## *II. Prevention*

# Compliance Program

## New FAR § 52.203-13

Ninety days after contract award, a large business must have:

- o an ongoing business ethics and business conduct training program
- o an internal control system

## *II. Prevention*

### Board Of Directors

### Gabig's Recommendation

Any corporation that derives the majority of its revenue from government contracts should have a Compliance Committee (not unlike it has an Audit Committee and a Compensation Committee)

## II. Prepare

1. Make “the day of infamy” and related decisions an off-site discussion topic
2. Lawyers are the equivalent to “emergency responders”



## II. Prepare

**3. Review insurance coverage and decide what is appropriate**

**4. Review indemnity in employment contracts and bylaws**

# III. Reaction

Master the facts before the government — complete an internal investigation

- “Damage assessment” vital
- Present “solution” to Govt before Govt dictates

# III. Reaction

## Internal Investigation Should Be Independent

- *Appears more objective*
- *Distances senior management*
- *Use lawyers to protect report as attorney-client privilege*

### III. Reaction

- Multiple agency involvement
  - *Global settlement preferred but difficult to arrange*
- Timely responses to agency vital for appearance of cooperation

# III. Reaction

- Risk of Obstruction of Justice
  - *Arthur Andersen*
- Notify insurance carrier
- Need for Board involvement
- Manage shareholder concern
- If public company, SEC complications

# III. Reaction

- Lead Counsel pursues an acceptable outcome
  - *DOJ (declination or deferred prosecution)*
  - *Regulators (no action)*
  - *Civil law suits (settle)*
  - *Suspension & Debarment (avoid)*



# III. Reaction

## DOJ's Corporate Fraud Task Force *"Aims High"* – Convictions 2002-6

□ CEOs	82
□ Presidents	85
□ Vice Presidents	102
□ CFOs	36

# III. Reaction

## Factors Considered By The Debarring Official

-- Whether the contractor had effective standards of conduct and internal controls systems in place at the time.

# III. Reaction

## **Factors considered by the Debarring Official (*continued*)**

-- Whether the contractor brought the activity to the attention of the government in a timely manner

# III. Reaction

## **Factors considered by the Debarring Official (*continued*)**

-- Whether the contractor has fully investigated the circumstances surrounding the cause for debarment

# III. Reaction

## **Factors considered by the Debarring Official (*continued*)**

-- Whether the contractor  
cooperated fully with Government  
agencies during the investigation

# III. Reaction

## **Federal Sentencing Guideline §8B2.1. Effective Compliance and Ethics Program**

“Such compliance and ethics program shall be reasonably designed, implemented, and enforced so that the program is generally effective in preventing and detecting criminal conduct. The failure to prevent or detect the instant offense does not necessarily mean that the program is not generally effective in preventing and detecting criminal conduct.”



# Concluding Thought

***Occupational Hazard*** – When you do business with the Sovereign, you risk incurring the Sovereign's wrath.

Treat like any any occupational hazard:

1. Prevent
2. Prepare