



1997

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Recommended Citation

Stanley Sporkin, *Lawsuits against the Public Corporation*, 50 SMU L. Rev. 27 (1997)
<https://scholar.smu.edu/smulr/vol50/iss1/6>

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Speech

LAWSUITS AGAINST THE PUBLIC CORPORATION

*Stanley Sporkin**

I. INTRODUCTION

I thank you for your invitation. I enjoy coming to Dallas to be with my former colleague and dear friend, Professor Marc Steinberg. As a long time observer of this nation's magnificent free market system, I very much appreciate the opportunity to discuss its various aspects.

My topic today is—suits against the public corporation—how to deal effectively with them. I am sure as corporate counsel, you look for someone to come forth with an inoculation against the common lawsuit, the equivalent of a flu shot.

Even though recently there has been some litigation reform measures enacted and possibly some more to come, the lawsuit will still be with us for the rest of our lives.

I am not saying that just because, as a judge, I have a vested interest in the litigation process. If the lawsuit disappeared I suppose I would still find something to do, perhaps just talking about the good old days. Sort of reminds me of the G.E. commercial where someone mentions changing a light bulb and a youngster says, "Changing a light bulb, why would anyone want to do that?" Well, while I know each of you would like to hear the words "lawsuit, what's that," I think we might be engaging in a bit of wishful thinking.

This does not mean there is nothing we can do now to lessen the impact of litigation. Indeed, I believe there is much that can be done. I would suggest a three prong attack consisting of (1) a litigation avoidance program; (2) a litigation monitoring and settlement program; and (3) a lessons learned and reform implementation program.

* The SMU Law Review Association was honored to have the Hon. Stanley Sporkin, U.S. District Judge for the District of Columbia, former Director of Enforcement of the Securities and Exchange Commission, and former General Counsel of the Central Intelligence Agency, as the keynote speaker at the 4th Annual SMU Corporate Counsel Symposium on October 18, 1996, in Dallas, Texas. Judge Sporkin graciously allowed the Association to reprint his speech.

II. LITIGATION AVOIDANCE PROGRAM

The first step in this program is to make sure your corporation has adopted a comprehensive litigation avoidance program. The more effective the program, the more likely the chances of being sued will be reduced.

What is needed here is a program that consists of periodic legal and financial audits. While much is known about financial audits, the same cannot be said of legal audits.

A public corporation should at least yearly make a detailed survey to determine what laws apply to it. When the survey has been completed, it is then incumbent upon the corporation to put in place mechanisms to assure compliance with all applicable laws. Be particularly mindful of environmental, safety, antidiscrimination, antitrust, and federal and state securities and banking laws. The Foreign Corrupt Practices Act must also be kept in mind. If any additional incentive is needed to establish a compliance mechanism, I invite your attention to the U.S. Sentencing Commission's Corporate Sentencing Guidelines. The guidelines that pertain to corporations also provide for lower guidelines sentencing where a corporation has established an effective system of compliance.

On this point, I have been advocating for some time the establishment of a new corporate position entitled "Business Practices Officer" or "BPO." Last year in a program sponsored by the Conference Board, I described the position in these terms:

This would be a corporate official whose duties would be analogous to those of a governmental Inspector General. The BPO would be responsible for seeing that the corporation conducted appropriate legal and financial audits and for assuring compliance with all applicable legal constraints. The BPO would investigate allegations of misconduct received from both internal and external sources. A hot line component could be an added feature. This position would be tenured and not be in the succession line for a higher corporate position. The independence of this position must be assured by both contract and the corporate culture. The officer would report directly to a truly independent audit committee.

Another aspect of the litigation avoidance program consists of implementing an alternative dispute resolution (ADR) system. All corporate contracts should be reviewed to assure an arbitration or an ADR clause has been inserted if you determine it is in the best interests of the corporation to take that route. Courts have paid great deference to arbitration clauses even with respect to various forms of employment disputes. Choice of law and change of venue clauses should also be considered for inclusion in contracts. Make sure all your contract forms are kept up to date. If a provision becomes obsolete, remove it from the contract and insert the new relevant provision.

The litigation avoidance program also entails that as corporate counsel, you closely monitor the corporation's various activities. As counsel you

must insist on receiving information about potential risks and potential failures. Ask the right questions of management officials. Read the business periodicals so you will be conversant with the latest rage on Wall Street. For example, investments in derivatives have been a source of considerable problems to many corporations. If your corporation is engaged in such transactions, insist on the corporation retaining its own independent adviser to evaluate the proposed investment package. Be cautious and very skeptical where your advice is coming from the packager or seller of the instrument. Have it reviewed by your own adviser.

Make sure you have access to the reports being generated by the corporation's internal compliance system. Request reports on complaints received; a hot line, if feasible, should also be implemented. If the corporation has a monitoring system, make sure the information turned up by the system is used. For example, in a recent case, the corporation had a taping system, but nobody took the time to listen to the tapes which turned out to be quite revealing.

III. LITIGATION MONITORING AND SETTLEMENT PROGRAM

Once a corporation has been sued, you must keep your directors and management fully informed and provide periodic assessments as to what the corporation's exposure is.

In my experience I found too little oversight is paid to corporate litigation. You must inform the Board of all material litigation—the sooner the better. Indeed, the Board should be informed at the point where litigation is first threatened.

Complaints from customers or clients must be carefully reviewed by compliance personnel, and where complaints are material and a strong inference that a suit may be forthcoming, immediate action must be taken. That is, the merits should be promptly investigated and, where appropriate, steps taken to satisfy the aggrieved party. In addition, where appropriate, steps should be taken to put in some new safeguards to prevent a recurrence of the activity that prompted the lawsuit.

At the inception of litigation and throughout its existence, a continuous settlement assessment must be made. The questions that must be asked are the following:

1. What are the merits of the lawsuit?
2. How much is it going to cost to litigate the case to its conclusion?
3. How much is it going to cost to settle the litigation?
4. What is the projected risk for others filing similar lawsuits?

When your corporation is being investigated or sued by the government, the risk analysis is even more intensive. You might have to bring into play your crisis management team. If this is a serious case, you possibly will be called upon to institute immediate reforms to make sure the offending conduct has ceased and the persons responsible for the infrac-

tions have been disciplined or replaced. You must assure that your various constituencies are being kept informed as to the underlying conduct.

When your corporation is contemplating instituting a major lawsuit, you must assess the chances of success and whether the lawsuit is the best way to achieve your objective. A careful risk-benefit analysis must be made. Ask the questions: (1) how much is it going to cost to litigate the case to its conclusion; and (2) will the monetary returns justify the anticipated costs?

The possibility of settlement should be carefully considered. You should always have an exit strategy, namely how do you ultimately envision the lawsuit being resolved. Be wary when the proponents of the lawsuit say it is not the cost but the principle that counts.

If there is a regulatory component to the case, consideration must be given to making a timely report to the governmental agency or agencies having jurisdiction.

During the course of any lawsuit, you must inform management and the Board's Legal and Audit Committee of all aspects of and changes in the litigation. The directors must be consulted at all major points of the lawsuit. As house counsel, you should be continuously assessing the chances of settling the litigation on terms favorable to the corporation. Where you have engaged outside counsel to litigate the case, you must closely monitor the progress of the litigation to assure all efforts are being made to settle the case. Do not let outside counsel fall in love with the case. Indeed, there may be occasion where you might want to engage another outside counsel to obtain a second opinion as to whether the case should be settled. At appropriate times during the course of the litigation, directors' presence at settlement discussions might be quite beneficial to resolving the case. Yes, I said directors. I remember one case where a corporation's directors attended a settlement conference in my chambers, and shortly thereafter, the case was promptly settled and the bleeding stopped. Indeed, there are judges that insist a corporate official with authorization to resolve the matter be present at settlement discussions. I personally welcome a businessman's presence at settlement discussions.

IV. LESSONS LEARNED AND REFORM IMPLEMENTATION PROGRAM

All too often after a lawsuit has been concluded, the champagne bottles are corked and the case is closed. Little more, if anything, occurs with respect to the litigation. In my view, this is the wrong approach to take. I would suggest that corporate counsel review the entire record to determine what lessons can be learned from the litigation and what, if any, reform measures must be instituted. The last thing you want is to have the conduct repeated. It is one thing to be blindsided by a lawsuit. It is entirely something else to be sued a second time because the cause of the problem has not been corrected. If a corporation has a problem with

derivatives, steps must be taken to assure it does not recur. This would be the same where a corporation has had to make a settlement to resolve an employment discrimination or hostile work environment case.

Litigation is sometimes necessary, and a corporation should always be prepared to defend a lawsuit or bring one where necessary to protect corporate assets or its integrity. Having said that, litigation should be avoided wherever possible. It is costly, and often a carefully crafted settlement can obtain better rewards for the corporation. Generally speaking, major corporate litigation should be conducted by outside counsel with the close assistance of house counsel. To repeat the old bromide, an individual who litigates his or her own case has a fool for a client.

V. CONCLUSION

These are a few suggestions that should prepare you for dealing in a more effective way with litigation. Remember to avoid lawsuits where possible, settle them at an early stage when practicable, and by an appropriate lessons-learned evaluation, make sure the underlying conduct does not recur.

I thank you for allowing me to share these views with you.

