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# Damn the Torpedoes? Key takeaways from the DOJ's New M&A "Safe Harbor" Policy

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**Damn the Torpedoes? Key takeaways from the DOJ's New M&A "Safe Harbor" Policy** [1]

**October 5, 2023 -** Yesterday, Deputy Attorney General Lisa Monaco unveiled the previewed changes to the U.S. Department of Justice's guidance on pre- and post-acquisition due diligence, announcing a new, Department-wide "Mergers & Acquisitions Safe Harbor Policy." [2] The key aspects of the new policy are:

- "Going forward, acquiring companies that promptly and voluntarily disclose criminal misconduct [at the newly acquired company] within the Safe Harbor period, and that cooperate with the ensuing investigation, and engage in requisite, timely and appropriate remediation, restitution, and disgorgement – they will receive the presumption of a declination [to prosecute]."
- "To ensure predictability, we are setting clear timelines. As a baseline matter, to qualify for the Safe Harbor, companies must disclose misconduct discovered at the acquired entity **within six months from the date of closing**."
- This deadline "applies whether the misconduct was discovered pre- or post-acquisition."
- "Companies will then have a **baseline of one year from the date of closing to fully remediate the misconduct**."

There will be room for some accommodation of particular facts or circumstances, although this could either lengthen or shorten the reporting expectation:

- "Both of these baselines are subject to a reasonableness analysis because we recognize deals differ and not every transaction is the same"
- But "companies that detect misconduct threatening national security or involving ongoing or imminent harm can't wait for a deadline to self-disclose."

The new Safe Harbor Policy also includes important exceptions to the DOJ's otherwise harsher stance on aggravating factors and recidivism:

- "For transparency, we are making clear that aggravating factors will be treated differently in the M&A context. The presence of aggravating factors at the acquired company will not impact in any way the acquiring company's ability to receive a declination."
- "Unless aggravating factors exist at the acquired company, that entity can also qualify for applicable VSD [Voluntary Self-Disclosure] benefits, including potentially a declination."
- "Finally, misconduct disclosed under the Safe Harbor Policy will not affect any recidivist analysis at the time of disclosure or in the future. Put another way, any misconduct disclosed under the Safe Harbor Policy will not be factored into future recidivist analysis for the acquiring company."

There are some important exclusions:

- The new policy "will only apply to criminal conduct discovered in bona fide, arms-length M&A transactions."
- "The Safe Harbor does not apply to misconduct that was otherwise required to be disclosed or already public or known to the Department."
- "Nor will anything in this policy impact civil merger enforcement."

Monaco's key takeaways included that "**Compliance must have a prominent seat at the deal table if an acquiring company wishes to effectively de-risk a transaction.**" She cautioned that "if your company does not perform effective due diligence or self-disclose misconduct at an acquired entity, it will be subject to full successor liability for that misconduct under the law." She also tied the new policy to the broader "**compliance convergence**" trend we have been observing, in which anti-corruption enforcement is a national security priority and enforcement policies for other national security priorities – including investigation and prosecution of sanctions and export controls evasion – are being brought in line with anti-corruption enforcement.

**Key Takeaways for Buyers and Sellers:**

- **The new policy seeks to increase the return for companies willing to invest the time and effort to conduct meaningful, risk-based pre- and post-acquisition due diligence:** While perhaps obvious, for compliance professionals looking to justify an increase in resources applied to pre- and post-acquisition compliance due diligence, the new Safe Harbor policy is meant to help. Monaco stressed that "In a world where companies are on the front line in responding to geopolitical risks – we are mindful of the danger of unintended consequences. The last thing the Department wants to do is discourage companies with effective compliance programs from lawfully acquiring companies with ineffective compliance programs and a history of misconduct. Instead, we want to incentivize the acquiring company to timely disclose misconduct uncovered during the M&A process."
- **In practice, it will likely be easier to buy time pre-acquisition than post-acquisition:** Post-closing, the clock starts ticking on the six-month timeframe for post-acquisition due diligence and the one-year timeframe for designing and implementing remedial measures. Even with the promise of a reasonableness-based extension of time for large or complicated deals, the only certain way to buy time to collect and analyze additional data is to conduct national-security related due diligence (anti-corruption, economic sanctions, and export controls, among other topics) as early as possible in the due diligence progress. Since problems in these areas can also significantly impact deal value and structure, there are benefits to doing so anyway. Sellers can help avoid last-minute delays by anticipating and preparing for due diligence questions on these issues.
- **Pre-acquisition due diligence should continue to include questions, and related purchase agreement protections, regarding the existence of ongoing investigations of the target:** Although it is already a standard practice to ask target companies if they are aware of ongoing investigations, the new Safe Harbor Policy's exclusion of matters that the DOJ already knows about underscores the importance of this practice. Even then, there is an unavoidable risk that there is an ongoing DOJ investigation about which the target is not aware, but being sure to ask the right questions, building in purchase agreement protections, and if necessary, setting aside in escrow funds to cover investigative costs and anticipated fines or other penalties remain very important.
- **Companies going into a selling process should expect additional questions:** One thing that sellers, including Private Equity firms looking to sell portfolio companies, should and can anticipate is that the time to prepare for

questions about anti-corruption, economic sanctions, and export controls compliance is before entering a selling process. Anticipating buyers' questions and buyers' incentives under the new Safe Harbor Policy will be important to maximizing sellers' value and avoiding last-minute delays in responding to compliance-related due diligence questions.

- **The need for risk-based, reasonably prompt integration remains:** The reality remains that buyers will still be limited pre-close to what sellers choose to provide them. The possibility for post-closing surprises remains; when such post-close surprises do arise, the clock will already be ticking and – consistent with parallel DOJ guidance that companies should increase the speed of internal investigations – buyers will still need to move quickly to identify root causes, remediate, and determine whether to make a voluntary disclosure within the baseline time periods provided.
- **Purchase agreement terms regarding post-closing liabilities remain critical to protecting acquirers' financial interests:** As with declinations awarded through the DOJ's Corporate Enforcement Policy, companies that receive a declination under the new Safe Harbor Policy will nevertheless still be required to pay appropriate restitution and disgorgement. Moreover, since the acquired entity (if still in existence) may not qualify for a declination if aggravating factors are present, it may also be subject to a criminal fine. Given these concerns, it is critical companies continue to include appropriate financial protections in purchase agreements that ensure they are adequately protected in the event they uncover misconduct that results in costly investigations, disgorgement, financial penalties or other costs.

Will the new Safe Harbor Policy mean "full steam ahead" for M&A activity with a clear path forward for avoiding prosecution with proper pre- and post-acquisition due diligence? Possibly. Voluntary disclosure is still a difficult decision to make, in that it is impossible in real life to conduct a controlled experiment. The deadlines, even with room for reasonable accommodation, will be difficult to meet for any significant, international acquisition, and, while there is a presumption of a declination for the acquiring entity, there is no guarantee that it will not suffer financial consequences as a result of a fine for the acquired entity. But providing clear expectations across the DOJ's divisions around which companies can anchor their diligence efforts and decision-making about acquisitions and disclosure is a welcome development.

Many companies have already increased their pre-acquisition compliance due diligence efforts and post-closing compliance integration, particularly in the areas of anti-corruption and trade controls. These companies are ahead of the curve in that their approach is directly in line with where the DOJ is expecting companies to go in terms of pre- and post-acquisition due diligence. For those behind the curve, now is the time to reassess current processes and reevaluate the value of compliance due diligence in light of the new Safe Harbor policy.

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1 On August 5, 1864, the Battle of Mobile Bay was fought during the American Civil War. The battle was a victory for the North, in large part due to then-Rear Admiral David Farragut's decision to ignore Confederate mines (then called torpedoes) in the bay, purportedly shouting "Damn the Torpedoes! Full Speed Ahead!" U.S. Library of Congress, Today in History – August 23 (commemorating the day the Confederate fort in the bay surrendered). ^

2 U.S. DOJ, *Deputy Attorney General Lisa O. Monaco Announces New Safe Harbor Policy for Voluntary Self-Disclosures Made in Connection with Mergers and Acquisitions* (Oct. 4, 2023) (emphasis added in the quotes that follow). ^

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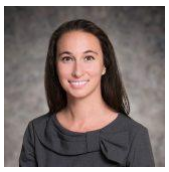

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