

New Financial Crimes Self-Reporting Policy Has Risks and Rewards

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New federal policies for corporate enforcement, voluntary self-disclosure, and cooperation guidance for financial crimes provides a strong incentive for companies, boards of directors, stakeholders, and shareholders to immediately disclose potential insider corporate malfeasance.

The US Attorney’s Office for the Southern District of New York—home to the largest financial institutions in the country and the prosecutor for most of the country’s financial crimes and public corruption cases—[announced the policies](#) on Feb. 24. A company will be shielded from criminal liability if it self-reports misconduct in that it will:

- Be immediately eligible for a conditional declination letter (stating that the government won’t prosecute the company)
- Receive a “final” declination letter if the company cooperates with the government to remediate the misconduct

In other words, self-reporting puts the company on a pathway toward guaranteed avoidance of criminal charges.

Compliance as Agent

A company must disclose the illegal activity to be eligible for a declination letter, even if the news media has reported the activity before the government agency makes a formal inquiry. The company must not be aware of a government investigation and the news media, for example, must not have reported a government investigation into the criminal activity.

This means that, at least for larger businesses, compliance is the watchdog geared toward investigating potential illegal activity, preparing the results of that investigation, and delivering that information to the US Attorney's Office. Aside from identifying the individuals involved in the illegal activity, as well as witnesses who may have material information, the company must:

- Share non-privileged factual results of internal investigations
- Provide all relevant documents and materials wherever located
- Facilitate the participation of employees and other agents of the company for government interviews as well as their participation in grand jury proceedings

For a period of three years, the company also must bring to the government's attention "all credible evidence or allegations of criminal conduct by the company or any of its employees that relates to violations of US laws." This means the company must accept self-imposed heightened evaluation of its policies and practices and employee conduct that rises to the level of even an allegation of criminal wrongdoing for three years after the initial disclosure. There is no guarantee that the reporting of future allegations or criminal conduct will result in an additional declination letter.

The heightened level of evaluation of internal conduct requires providing the government with ongoing records and information the company otherwise might not have disclosed and, in turn, could be waiving defenses by those disclosures. Consistent with routine practice in the Southern District of New York, the government might further require the company to agree to an independent monitor to ensure the company is living up to its disclosure obligations.

There is always the risk that, where the company has reported prior wrongdoing, statutes that impose criminal liability for patterns of misconduct will expose the company to serious federal criminal liability. In that situation, the government already will have required the company to hand over records from the initial self-disclosure that can help establish predicates for holding the company criminally liable for conduct revealed in the subsequent report.

Self-disclosure of criminal conduct isn't a shield from investigation or prosecution by the New York State AG's Office. The Martin Act (New York General Business Law §352-c) grants state prosecutors at the New York AG's Office extraordinary powers in securities fraud cases, requiring no proof of intent to defraud or even actual deception. This makes New York one of the most challenging jurisdictions for defending against securities-related charges.

As a practical matter, voluntary disclosure under the new policy with the Southern District of New York also likely means voluntary disclosure with the New York State AG. However, the AG's office doesn't provide the same benefits or cooperation regime and could take a very different view as to the company's liability and punishment.

C-Suite Implications

An employee trading in material non-public information can expect to be reported to law enforcement. However, the new Southern District of New York policies are oriented to less common, more sophisticated alleged criminal conduct where the company might otherwise have less incentive to report.

While no company should protect criminal conduct at any level of the organization, it's essential to carefully consider the facts underlying the conduct at issue and what comes along with cooperation under these rules, especially when the stakes are particularly high. Typically, this scenario exists when the allegations are oriented toward the C-suite and when company must decide whether to try to save itself by extracting the executives.

The 2019 federal [prosecution](#) of Gordon Coburn and Steven Schwartz, the former president and chief legal officer of New Jersey-based Cognizant, respectively, provides insight here. Coburn and Schwartz were indicted for violating the Foreign Corrupt Practices [Act](#) by allegedly approving a \$2 million payment to an Indian government official to help obtain a construction permit in India for an office building.

Within two weeks of learning of the payment, the Cognizant board made a disclosure to the US Attorney's Office and received a declination letter for the company. A federal indictment against the executives was summarily [dismissed](#) last year. In effect, from a legal perspective, the Department of Justice found that the executives had committed no crime that it could establish.

In high-stakes scenarios, a common reaction is to fully cooperate with the government. This approach is often viewed to be in the best interest of employees, shareholders, and stakeholders. However, certainty of a conditional declination letter doesn't mean the company has avoided litigation costs and risks, either in the form of subsequent criminal action and penalties or in terms of disruption to management. Where there might be real defenses alleged wrongdoing, the risks are even more enhanced.

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