

White-Collar Defense

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EXECUTIVE SUMMARY: In this month's roundtable, our panel of experts discusses the government's increased use of deferred prosecution agreements, which often put corporate defendants into the difficult position of agreeing to terms that are more severe than they would have received had they pled guilty; how the government continues to insist on the waiver of attorney-client privilege as a sign of cooperation; and the trend of pressuring corporations not to pay attorneys' fees or enter into joint defense agreements when executive employees are under investigation.

The panelists are Raymond Marshall of Bingham McCutchen; Leslie Caldwell and John Hemann of Morgan Lewis & Bockius; Stephen Freccero of Morrison & Foerster; and Patrick Hanly of Nossman Guthner Knox & Elliot. The roundtable was moderated by Custom Publishing Editor Chuleenan Svetvilas and reported for Barkley Court Reporters by Krishanna DeRita.

MODERATOR: Is the government's use of deferred prosecution agreements increasing?

CALDWELL: It's definitely on the rise. The government has figured out that in most contexts, it does not actually have to indict a company to get everything it would get if it did indict the company. Also, the government can avoid certain collateral consequences to the company like the company being debarred from federal programs or going out of business.

Now that it's gotten an appetite for deferred prosecutions, the government is now perhaps being too quick to say, "Hey, why don't we enter into a deferred prosecution agreement?" in cases where there may never previously have been a criminal prosecution. On the defense side, the first goal is to try to keep the government out of that mindset and understand that there's no reason to do anything to this company.

MARSHALL: I looked at a couple of years of deferred agreements, and tried to catalog the various collateral consequences. Some of the terms in the agreements are as onerous as if the company had pled or been found guilty—not only the financial fines, but a lot of the injunctive relief and oversight conditions that have been imposed track the SOX oversight requirements. The waiver issue and the terms of cooperation are also of concern. A number of the terms are extremely negative and have the potential to result in adverse consequences during the 18-month or three-year period that prosecution is deferred.

CALDWELL: The terms have gotten a lot more onerous. I remember

when [I was working for the government and] we were deciding what to do with Arthur Andersen. We were discussing a deferred prosecution, which Arthur Andersen ultimately declined to do, but the terms would have been far less onerous than, for example, the deferred prosecution with KPMG where the factual admissions were almost tantamount to a guilty plea.

HANLY: And that can lead to civil consequences as well. Many times in these agreements you have to admit to a certain factual basis, and then civil litigants who are trying to sue your client can use that information in the civil litigation. While the company might avoid criminal prosecution, they then have leapt right out of the frying pan into the fire in a civil litigation context. So, while they can continue to operate under a deferred prosecution agreement, they end up jumping out of a criminal prosecution and into defending a shareholders' lawsuit.

Given the huge costs associated with civil litigation these days, companies must think long and hard before readily agreeing to a deferred prosecution agreement. Sometimes it makes more sense to fight the government than just roll over and end up fighting multiple plaintiffs in the civil courts.

HEMANN: The admissions that are required in a deferred prosecution agreement are often much more extensive and more detailed than the admissions that are required in order to plead guilty. The government will say, "Look, in a deferred prosecution context, you need to not only admit this, but also these four other things." You need to describe the conduct in more detail; you need to promise as part of the agreement

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that you will never back away from it. A provision that is commonly included is that you will never dispute in any form in any way that this conduct took place—you won't take any position in any litigation that is contrary to your factual admissions or you will be in breach of the agreement with the government.

MARSHALL: One of the problems is the unilateral determination by the government whether a breach has occurred. For the most part, the government alone makes the determination that you've breached the agreement. They will look at pleadings that you have filed in civil or administrative proceedings to determine whether you have come close to contradicting or undercutting the statement of facts that you've agreed upon. That's a scary proposition.

HANLY: Failure to accept a deferred prosecution agreement can have dire consequences. Contrast what happened to Arthur Andersen, who turned down the deferred prosecution agreement and is now out of business, with a company like MCI, which entered into such an agreement, and now their stock is in play. So even though MCI agreed to a very onerous deferred prosecution agreement, it is still alive and working, whereas Arthur Andersen is not. And so as bad as it is, it's at least a lifeboat for the company.

HEMANN: I always feel a little cautious about using Arthur Andersen as the example, because it was unique in several respects. Companies do still plead guilty and take criminal convictions, particularly in antitrust and health care, and continue to exist and thrive.

Arthur Andersen had a number of problems in other cases leading up to the criminal trial, and they were also saddled with the ongoing substantive problem of Enron. They had the obstruction problem plus the fact that they had counseled Enron in connection with some of the deals that caused problems for Enron. They did suffer the ultimate punishment, but corporations might be able to get away with better deals if they don't reflexively take the deferred prosecution.

FRECCERO: Deferred prosecution is both an opportunity and a potential minefield for a company. If the company looks at the evidence and determines that criminal charges could be brought, then deferred prosecution provides an opportunity to avoid all the collateral consequences that can come with simply being charged with a crime.

I wonder, however, if the increased use of deferred prosecutions will make it more likely that the government takes a position of "we think we could charge this company because the risks are so high for the company." The company will feel that it cannot afford to take the chance and will enter into a deferred prosecution agreement.

MARSHALL: Clients just have to be aware as to what it means. Think about the collateral consequences of going to trial. The upside is, you get certainties. If you can settle the civil suit and pay \$38 million, you not only just survive, but the stock goes up the next day. Why? Because they have certainty.

Our corporate clients want the opportunity to be there tomorrow. You don't want two years of being in the press. You don't want three years of having executives and your work force being demoralized and worried about what happens to them.

FRECCERO: Do you really think in all those cases in which the issue of

deferred prosecution is being discussed, the government would actually bring criminal charges and see the proceedings through?

MARSHALL: No, not in all. But it's high-stakes poker. I believe that the government has gone overboard. There are cases where clients should be less agreeable, where they should stand and fight and force the government to make its case. But it's not my life at stake. It's not me who has to wake up in the morning worried about whether I will see my children the next day. It's not me worried about whether my company will be able to maintain its employee workforce.

HEMANN: The problem is that in this high-stakes poker game if the government loses its hand, it lives to play another day. And companies feel that they may not live to play another day. So it's not an even playing field. The routine use of deferred prosecution agreements has lowered the burden on the government: They get everything they want; they don't have to go to trial; they don't have to prove the case. And the lawyer for the company and the company are able to declare that they've avoided prosecution. But at what cost?

CALDWELL: I've seen situations already, even in my short time in private practice, where prosecutors put the deferred prosecution agreement on the table well before they've developed the evidence that could possibly be used to convict the individuals at the company, much less the company itself. So it does seem that the Thompson memo and DOJ policy view deferred prosecution as something that's probably supposed to be used in more limited circumstances than currently it's being used.

HANLY: The amounts of money that the companies are settling for are staggering. Under the Thompson memo, the government is requiring the company to do the investigation and give the government the information it obtains in order to enter into this deferred prosecution agreement. It's almost like the company convicted itself, paid a huge sum of money, and then went on its way.

FRECCERO: The difficult part is that companies are called on to make these kinds of decisions at a point in time where the facts are not clear. Often the government is pushing for some sort of early response from the company, precisely because it hasn't been able to muster the resources or hasn't been in the investigation long enough to draw its own conclusions. Anyone who has been involved in a long or difficult investigation will tell you that sometimes you don't know the full facts until after you have reviewed thousands of documents and interviewed hundreds of people.

HANLY: Are you all finding that in both corporate and individual cases, that the government has been pushing or requesting a decision on a plea offer without providing full discovery early on in the case?

MARSHALL: In the last few months I've had two of those "preindictment" conversations. They were not invitations to negotiate. What the government says is something along the following: "You can come and tell us your side of the story. We are willing to entertain an early resolution. This means that we'd expect that you will plead to this felony or have a deferred prosecution agreement on the basis of the assumption that what we have said is true. But we are not even going to tell you

and disclose all that we know. But we are going to give you a general overview that we could charge you with X, Y, Z, and X, Y, Z is a general statement without detail. If you want to come in and tell me more about those details, fine. We are open to resolving it at this stage, but if not, that's fine, too." So it's very one sided.

MODERATOR: How has attorney-client privilege been affected?

FRECCERO: The waiver of attorney-client privilege is the one thing that the government gets out of a deferred prosecution that it would never get out of an indictment. It's far more difficult to obtain attorney-client communications in court than it is to demand it at the outset of an investigation. Ultimately, it may prove to be a misguided policy for the government. It is the prime motivating factor for investigators to start talking about a deferred prosecution agreement because, from the government's perspective, there's a strong belief that free access to privileged communications results in evidence that they would not otherwise be able to obtain.

CALDWELL: The privilege waiver is another area where there's a disconnect between the policy reasons for requesting the waiver and what's actually happening in practice. The idea is, if the case is extraordinarily complicated and you've conducted an internal investigation, you can waive the privilege and get the government all that information easily so that they don't have to negotiate immunity with every single person interviewed and do a long investigation and figure out what happened when people are taking the Fifth and not talking.

It's really supposed to be the exception, not the rule, that you ask for a privilege waiver. Now the government, almost from your first meeting, is asking you to waive the privilege.

MARSHALL: They are insisting on the waiver very early on, and they do view waiver as a sign of cooperation. It's a sign of noncooperation if you refuse or want to argue jurisprudence, or the importance of the privilege to an effective criminal justice system.

HANLY: If you offer to provide the same information by turning over your internal investigation by way of attorney proffer, that's not good enough even though they would get the exact same information from the attorney as they would from the internal investigation. The government is riding the wave of big corporate scandals and they know that all the corporate clients are afraid. They are piggybacking on the deferred prosecution agreement, and one of the key things they want is the waiver of the attorney-client privilege.

FRECCERO: The Department of Justice recently issued a memorandum telling each respective U.S. Attorney's office to draft a policy outlining the circumstances and protocol for requesting that a company waive the attorney-client privilege. Each district is free to set up its own policy. I find this ironic because in sentencing, the mantra has been, "we want consistency throughout the country and the districts."

Ultimately, the courts will be weighing in on a lot of these issues. We are starting to see decisions as to what the implications are for such a waiver in the context of internal investigations where counsel for the company is talking to a company employee.

HEMANN: Waivers have an insidious effect on investigations. Every time

I give the *Upjohn* warning at the beginning of an interview, "We don't represent you, we represent the company, if the company decides to waive, then we all have to live with that," I know that I will not get the same kind of information and quality of information than if I were able to say, "I am your lawyer. I'm the company's lawyer. This conversation is privileged and will be used by the company to determine what happened. You should tell me everything."

I'm not proposing that that be the norm—that conversations with employees be privileged in all cases. But I'm not sure it really helps the government that much to routinely get waivers because they are not necessarily getting top-quality information as a result.

MODERATOR: Is there now a trend of pressuring corporations not to pay attorneys' fees or enter into joint defense agreements where executive employees are under investigation?

CALDWELL: I'm afraid so. This is another disconnect between the policy reason behind the Thompson memo and the actual application of the policy reason. In the bad old days, companies would pay attorneys' fees, enter into joint defense agreements, and the understanding would be that everyone would tell the same story or they would all demand immunity. These provisions were designed to stop that, because that essentially amounts to maybe not literal obstruction, but quasi-obstruction.

The whole idea of not paying attorneys' fees for culpable employees has been taken to the extreme and now the government is saying, "We don't want you to pay, and don't pay person X unless you are obligated by some provision of state law or corporate bylaws." So now these people have incompetent representation because they can't hire experienced counsel. They have to hire cousin Vinny who has no idea how to do it. They and the company could end up being worse off. And the government is not getting what they would get with competent representation.

HEMANN: It appears that the purpose is to pressure low-level employees to flip. For them, no job, no money, no information, so we have nothing to lose, and everything to gain by cooperating and doing it early.

HANLY: It also drives a wedge between the company and the employee because the employee is looking to the company for that support, and then the company is saying, "We are not doing anything for you," Then there is an "us versus them" mentality, which does not help the company at all.

MARSHALL: To me that's probably one of the most offensive aspects of where we are now, because it doesn't really encourage cooperation on the part of company, and it doesn't really generate disclosure. It generates ill will between the company and employees, and not just the impacted employees who might be subject to target, but the entire workforce.

FRECCERO: There's also a public policy issue. What's surprising to me is that many states long ago weighed in on these types of issues, certainly California, and decided that there's a duty on the company to defend, at least where the facts are not absolutely clear. If everyone were absolutely certain as to what had occurred, we wouldn't have an investigation. We'd go straight to the criminal proceedings. ■

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