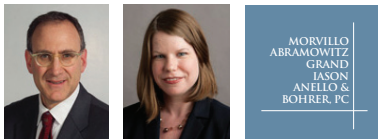


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Be Careful What You Wish For: How Deferred and Non-Prosecution Agreements Can Be Used in Civil Litigation



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A company under criminal investigation by federal prosecutors often seeks to resolve the investigation by entering into a deferred prosecution agreement (DPA) or non-prosecution agreement (NPA). In this way, the company can avoid the harm of an indictment and trial. At the same time, such agreements impose burdens and have collateral consequences. DPAs and NPAs commonly require substantial governance changes, an admission of wrongdoing, acceptance of a statement of facts describing the company's criminal conduct, and a prohibition on public statements contradicting admissions in the agreement.

As this article will explore, these requirements often place significant constraints on the company in subsequent civil litigation, as the statement of facts constitutes an admission that may be used to establish the company's liability. Factual admissions made as part of a DPA or NPA generally are admissible as statements by a party-opponent, and plaintiffs have used these admissions to supply proof of the defendant company's liability in civil complaints and motion practice.

A recent decision in New York State court, *Borst v. Lower Manhattan Development Corp.*,¹ at first blush offers hope that admissions made as part of DPAs or NPAs may not be admissible in subsequent civil litigation. The *Borst* court declined to admit into evidence a statement of facts agreed to by defendant Bovis Land Lease LMB, Inc. (Bovis) as part of an agreement with the New York County District Attorney on the grounds that the document reflected inadmissible settlement negotiations. However, the Bovis agreement was written very differently than the typical federal DPA or NPA. Most importantly, Bovis's agreement did not require an admission of wrongdoing. While agreements with state authorities may leave a company more freedom to dispute key issues in civil litigation, it is unlikely that federal DPAs and NPAs will allow companies the same flexibility.

Current Use of DPAs and NPAs

The Department of Justice (DOJ) has issued Principles of Federal Prosecution of Business Organizations (DOJ Policy) that instruct prosecutors to enter into a DPA or NPA in circumstances "where the collateral consequences of a corporate conviction for innocent third parties would be significant."² Such agreements are designed to allow the company to remain in business, so as to preserve jobs and shareholder value, and increase the likelihood that victims will receive prompt restitution. The government seeks to achieve general and specific deterrence typically by requiring substantial changes to the company's governance and operations, requiring regular reports on the progress of those reforms from

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a compliance monitor or the company itself, and reserving the power to revive criminal charges if the company is deemed to be noncompliant.

DPA and NPA are most commonly used to resolve investigations concerning fraud and the Foreign Corrupt Practices Act, but in recent years, DPAs and NPAs have been seen in cases involving a wide variety of federal criminal statutes. In 2010, for example, the investigations concluded by DPAs and NPAs involved the Federal Anti-Kickback Statute in the context of drug and device marketing, the False Claims Act, antitrust laws, and the Bank Secrecy Act.

In a deferred prosecution, the government charges the corporation in a criminal information, which it agrees to dismiss at the end of a specified term if the corporation has complied with the terms of the DPA. Because it is filed with the court, a DPA is a public document. By contrast, an NPA does not arise from the filing of criminal charges, and the agreement will not be made public unless the prosecutors seek to publicize the result of their investigation or the company is required to disclose the agreement. The DOJ Policy leaves the specific provisions of DPAs and NPAs to the discretion of the office conducting the investigation, and in recent years the terms of the agreements have become more consistent.³ Most DPAs and NPAs include the following provisions:

1. Acceptance of a statement of facts describing illegal acts and/or an admission of wrongdoing;
2. Agreement that the company, its employees, and agents will not publicly contradict the statement of facts;
3. Cooperation with the government for the duration of the agreement, including the provision of documents and efforts to secure employee testimony;
4. Remedial efforts such as the enhancement of compliance programs, a corporate integrity agreement, and/or monitorship;
5. Fines and penalties;
6. Obligation to report future violations of the law;
7. Waiver of the statute of limitations; and
8. Acknowledgement that the government has sole discretion to determine whether the agreement has been breached, and, upon breach, the agreed statement of facts shall be admissible in a prosecution of the company.

Consequences of Entering into a DPA or NPA

The obligations imposed on a company as part of a DPA or NPA—particularly the cooperation and compliance requirements, which may cost millions of dollars—give rise to substantial financial and operational burdens. Additionally, entering into a DPA or NPA eliminates most opportunities for judicial review. Judges generally conduct little review of an agreement's terms and commonly are not involved with monitoring or evaluating the company's performance.⁴ Most, if not all, DPAs and NPAs provide that the prosecuting agency is the sole arbiter of the company's

compliance with the agreement. If, in the government's view, the company fails to comply with the agreement, the government may declare a breach and proceed with a criminal prosecution of the underlying offense, and may use as evidence the company's admissions and the information provided by the company as part of its cooperation obligation. If the company's DPA or NPA prohibits it from publicly contradicting the facts described in the agreement, it runs the risk that any of its public statements could be viewed by the government as a breach warranting the revival of criminal prosecution.

The risks of giving such broad discretion to the government can be seen in the case of FirstEnergy Nuclear Operating Company, which, in 2006, entered into a DPA resolving allegations that it knowingly made false statements to the Nuclear Regulatory Commission (NRC) concerning its inspection practices and the safety of the Davis-Besse Nuclear Power Station. As part of the agreement, FirstEnergy accepted responsibility for its conduct as set forth in a statement of facts detailing the company's unsatisfactory inspections, which led to unreported damage to the reactor lid. The company further agreed not to make public statements contradicting the agreement.⁵

FirstEnergy subsequently filed a claim in arbitration with its insurer, seeking coverage for its losses incurred while the damaged reactor was shut down for repairs. The company presented consultant reports which concluded that the company did not intentionally cause damage to the reactor and therefore was entitled to coverage. When the NRC learned of FirstEnergy's position in the arbitration, it demanded a statement from the company explaining the consultant reports in light of the admitted statement of facts in the DPA, and suggested that, if the two were not reconciled, the NRC would refer the matter to the DOJ as a breach of the agreement.⁶ Facing the unenviable choice of either foregoing its insurance claim (and avoiding prosecution) or being further prosecuted based on its own admissions, FirstEnergy chose the former course. The company renounced the problematic portions of the consultant reports and ultimately discontinued the insurance arbitration altogether.⁷ A court may have agreed with FirstEnergy that the consultant reports were not inconsistent with the DPA, but FirstEnergy had no ability to obtain judicial determination of that issue until after being indicted—a risk most companies will not take.

Use of DPAs and NPAs as Admissions in Subsequent Civil Litigation

The requirements that the company accept responsibility and refrain from making contradictory statements may have a major effect on civil litigation against the company. Factual admissions made as part of a DPA or NPA generally will be admissible as statements by a party-opponent under [Federal Rule of Evidence 801\(d\)\(2\)](#). That rule provides that, when offered against an opposing party, a statement made by that party, his agent or authorized representative, or a statement the opposing party has adopted or believed to be true, is not hearsay and is admissible if the court finds it is relevant. Most DPAs and NPAs contain a

provision qualifying the incorporated statement of facts as a statement adopted by the company. For example, agreements may provide that the “[Company] acknowledges and accepts as accurate the facts set forth in the Statement of Facts attached;⁹⁸ or the “[Company] admits, accepts and acknowledges responsibility for the conduct of its [Employees], as set forth in the Statement of Facts.”⁹⁹ Both of these provisions plainly indicate adoption on the part of the company.

In practice, the admissibility of statements made pursuant to DPAs and NPAs has been litigated during pre-trial motion practice. Before trial, courts have accepted the agreements as admissions and consider them as proof supporting plaintiffs’ claims, often finding that the agreement in question provides plaintiffs with sufficient evidence to survive a motion to dismiss. For instance, in *Davis v. Beazer Homes, U.S.A., Inc.*,¹⁰ plaintiff, a homebuyer who financed her mortgage through defendant Beazer Homes, alleged that the company artificially inflated the price of her home through deceptive lending practices. In its DPA, Beazer had admitted and acknowledged responsibility for fraudulent home loans that resembled the deceptive practices alleged by plaintiff. The court deemed the company’s admissions to be “a significant factor in addressing the plausibility of plaintiff’s claim,” and held that plaintiff’s complaint was adequately pled.¹¹ Similarly, in *Somerville v. Stryker Orthopaedics*,¹² the court denied defendants’ motion to dismiss based on Stryker’s NPA concluding an investigation into violations of federal anti-kickback law.

Plaintiffs have successfully used the admissions in a DPA in other pretrial motions as well. In one case, plaintiffs filed fraud and breach of fiduciary duty claims in state court against KPMG arising from tax shelter investments. KPMG sought removal under federal question jurisdiction, arguing that the litigation turned on a determination of the lawfulness of the tax shelters under federal law. The court rejected this argument and remanded the case, finding that KPMG’s acceptance of responsibility in connection with its DPA, in which it admitted that it sold fraudulent tax shelters, obviated the need to construe federal tax law to resolve plaintiffs’ claims.¹³

At the same time, the admissions in a DPA or NPA will not save a complaint if the admissions do not bind a party on key issues in dispute. In *Shalam v. KPMG LLP*,¹⁴ another case involving fraudulent tax shelters, the trial court denied a motion to dismiss, holding that the admissions made by defendant Hypo-Und Vereinsbank (HVB) in a DPA with federal prosecutors precluded, as a matter of law, a finding that HVB did not defraud plaintiff, a participant in an HVB tax shelter. The New York Appellate Division reversed, holding that the facts admitted by HVB established only that HVB committed fraud on the IRS; the admissions did not establish that HVB had defrauded plaintiff.

In sum, courts treat the agreed-upon statements of fact in DPAs and NPAs as admissions in civil litigation. These admissions are merely that—admissible against the defendant, but may not themselves be dispositive of liability, particularly when the admissions in the agreement do not correspond precisely with the conduct alleged in the complaint.

Borst: Non-Prosecution Agreement Is a Settlement Discussion, Not an Admission

In its recent decision in *Borst v. Lower Manhattan Development Corp.*, the Supreme Court for New York County took a different approach, treating the agreed-upon facts in an agreement between Bovis Lend Lease LMB (Bovis) and the District Attorney’s Office as settlement negotiations and thus inadmissible to prove liability in a subsequent suit. The holding relied upon the language of the agreement before it, which differed from a typical NPA or DPA.

In 2007, two firefighters were killed and 105 more were injured while battling a fire at the Deutsche Bank building near the World Trade Center site. Immediately after the fire, the District Attorney opened a criminal investigation into its causes, and concluded that the dismantling of the building’s standpipe led to the firefighters’ deaths and injuries. It found that Bovis, the contractor engaged in demolition work at the site, failed to maintain the standpipe as it was required to do. As a result of the investigation, the DA’s office “determined that it could institute a criminal prosecution” against Bovis for manslaughter.¹⁵

The DA entered into an agreement not to prosecute Bovis under which the company undertook to comply with a number of remedial financial and training measures and “acknowledge[d] responsibility for its actions.”¹⁶ The agreement further provided that Bovis “does not challenge the factual recitation of its conduct and that of its employees” as set forth in the DA’s statement of facts appended to the agreement (DA’s Statement). As part of its obligations under the agreement, Bovis also agreed that neither it nor its agents or employees would make any public statement contradicting the DA’s Statement—*except* in connection with civil proceedings related to the fire. The agreement stated that Bovis neither admitted nor denied criminal and civil liability. Bovis released its own statement, appended to the agreement, which acknowledged that the DA’s investigation “disclosed failures on the part of Bovis employees” and reiterated that Bovis does not challenge the factual conclusions of the DA’s office that certain of its employees failed to comply with their supervisory and maintenance obligations.¹⁷

The plaintiffs in *Borst*, firefighters injured in the fire, sued Bovis for damages. Plaintiffs moved for summary judgment, arguing that Bovis’s agreement not to challenge the DA’s Statement constituted an admission of the facts therein and established Bovis’s negligence. The court denied this motion. First, it held that because the DA had commenced a criminal investigation and was contemplating charging Bovis prior to its agreement with the company, the company’s agreement with the DA constituted a settlement of impending criminal charges. Because offers to settle a claim are inadmissible as proof of liability under New York’s evidence law, the agreement and any factual statements therein cannot constitute admissions by Bovis.¹⁸ In support of this conclusion, the court did not distinguish between statements made in compromise negotiations and evidence provided to prosecutors in the course of a criminal investigation. Rather, it cited a number of cases that concerned the admissibility of civil settlements in other civil cases.

The court also held that the DA's Statement was not admissible against Bovis because it was evident that the parties did not intend to bind Bovis to "admissions" outside of the criminal proceeding.¹⁹ The agreement explicitly acknowledged Bovis's right to take legal and factual positions contradicting the DA's Statement in any subsequent litigation to which the DA was not a party. The court relied upon *Callahan v. P.J. Carlin Construction Co.*,²⁰ in which it was held that plaintiff could not use stipulations made by defendant to settle OSHA violations as evidence of negligence because the parties specified that the stipulations were not to be taken as an admission in other proceedings.

Borst's Potential Impact

As construed by the court, the agreement in *Borst* was treated as analogous to a consent judgment in civil litigation. Consent judgments—under which the respondent agrees to a sanction but neither admits nor denies the substance of the allegations in the regulator's complaint—are not admissible in a subsequent litigation to prove the truth of the claims described therein.²¹ Like pleas of *nolo contendere*,²² consent judgments are not true adjudications of the underlying issues, and are thus not to be considered as evidence or precedent.²³

The salient features of Bovis's agreement with the DA are more similar to the features of consent judgments entered by the SEC and other regulators, rather than a standard DPA or NPA. First, Bovis, like the respondent in a consent judgment, neither admitted nor denied that it engaged in wrongdoing. Second, Bovis's agreement, like consent judgments, allowed the company to contest the facts underlying the agreement in subsequent litigation. Indeed, the comparison to a consent judgment is perhaps more persuasive than the analysis in *Borst*, which somewhat unconvincingly treated evidence gathered by the District Attorney in a criminal investigation as the functional equivalent of statements offered to settle a civil claim. Like a consent judgment, Bovis's agreement with the DA has given the company flexibility in subsequent civil litigation.

However, agreements like Bovis's that do not require a corporate defendant to admit wrongdoing are rarely accepted by federal prosecutors, limiting the reach of the *Borst* analysis. In 2008, the U.S. Attorney's Office for the District of New Jersey entered into five such agreements²⁴ with manufacturers of orthopedic implants, settling charges that the companies violated anti-kickback laws by giving lucrative consulting agreements to surgeons who used the companies' devices. As part of the agreements, each company "acknowledged responsibility for its behavior," but explicitly denied any wrongdoing. In December 2011, Alpha Natural Resources, Inc. entered into an NPA with the U.S. Attorney's Office for the Southern District of West Virginia, which allowed the company to deny liability concerning its mining operations at the Upper Big Branch Mine where an explosion killed 29 miners in April 2010. The agreement also allowed Alpha to resolve numerous outstanding citations for mine safety violations with no contest pleas.²⁵

Conclusion

Non-prosecution and deferred prosecution agreements that do not require admissions of guilt are likely to remain rare. The DOJ has made company admissions of culpability a hallmark of DPAs and NPAs. Both the New Jersey orthopedic implant agreements and the Alpha agreement have attracted scrutiny and criticism, and thus are likely to remain the exception rather than the rule.²⁶ Likewise, the validity of the SEC's practice of settling enforcement actions through consent judgments has been called into doubt.²⁷ Though in some circumstances a company may be able to structure a DPA or NPA so that the company is free to dispute key facts in civil litigation, a party entering into a DPA or NPA should understand that the agreement is unlikely to be so flexible. While DPAs and NPAs have enormous advantages over indictment and trial, such agreements almost certainly limit a company's options in subsequent litigation.

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¹ 2011 N.Y. Slip Op. 32372(U), No. 105375/2008 (Sup. Ct. N.Y. County Sept. 6, 2011).

² U.S. Attorney's Manual § 9-28.1000 (Aug. 2008).

³ See GAO Report to Congressional Requesters, *Corporate Crime: DOJ Has Taken Steps to Better Track its Use of Deferred and Non-Prosecution Agreements, but Should Evaluate Effectiveness*, GAO-10-110 (Dec. 2009), at 17 (GAO Report), available at <http://www.gao.gov/new.items/d10110.pdf> (noting DOJ's recent efforts to ensure consistency across agreements).

⁴ See GAO Report, at 25-26.

⁵ John Mangels, *Claim May Retrigger Criminal Probe: FirstEnergy's Insurance Case Contradicts NRC on Davis-Besse*, Cleveland Plain Dealer (June 8, 2007).

⁶ *Id.*

⁷ Tom Henry, *FirstEnergy Drops \$200 Million Insurance Claim at Davis-Besse*, Toledo Blade (Dec. 11, 2007).

⁸ See, e.g., Non-Prosecution Agreement between Sportingbet PLC and the U.S. Attorney of the Southern District of New York (Sept. 20, 2010), available at <http://www.gibsondunn.com/publications/Documents/sportingbet.pdf>.

⁹ See, e.g., Deferred Prosecution Agreement between Kos Pharmaceuticals, Inc. and the U.S. Attorney for the Middle District of Louisiana (Nov. 16, 2010), available at <http://www.gibsondunn.com/publications/Documents/KosPharmaceuticalsDPA.pdf>.

¹⁰ No. 08-CV-00247 (M.D.N.C. Nov. 17, 2009).

¹¹ *Id.*

¹² No. 08-CV-02443 (N.D. Cal. Sept. 4, 2009).

¹³ *Abrams v. KPMG, LLP*, No. 05-CV-03745, 2006 BL 29746 (D.N.J. Feb. 28, 2006).

¹⁴ 931 N.Y.S.2d 592 (App Div. 1st Dept. 2011). See also *Glazer Capital Management v. Magistri*, 549 F.3d 736, 748-9 (9th Cir. 2008), in which the court dismissed plaintiff's securities fraud claim when it determined that the admissions made in a company's NPA concerning its FCPA violations did not sufficiently evidence scienter on the part of defendants, the company's CEO and CFO.

¹⁵ Non-Prosecution Agreement between Bovis Lend Lease LMB, Inc. and the New York County District Attorney's Office (Dec. 22, 2008), available at <http://manhattanda.client.tagonline.com/whatsnew/press/2008-12-22/>

[Bovis%20agreement%20with%20Fire%20Safety%20Initiatives.pdf](#). The DA's statement appended to the NPA summarized the findings of the office's investigation and concluded that numerous others, including some New York City agencies, failed to conduct their duties and contributed to the conditions that caused injuries and death in the Deutsche Bank fire.

¹⁶ *Borst*, 2011 N.Y. Slip Op. 32372(U), at *2. The New York County District Attorney's Office has a policy regarding the criminal prosecution of companies similar to that of the Department of Justice. See Memorandum of Daniel R. Alonso, Chief Asst. District Atty., *Considerations in Charging Organizations* (May 27, 2010), available at <http://manhattanda.org/sites/default/files/Considerations%20in%20Charging%20Organizations.pdf>.

¹⁷ The DA's statement explained that Bovis employees created fraudulent documents and disregarded their obligations to maintain required safety standards. See Exhibit A to Non-Prosecution Agmt. between the District Atty. of N.Y. Cty. and Bovis Lend Lease LMB, Inc., dated Dec. 19, 2008 (on file with the authors).

¹⁸ *Borst*, 2011 N.Y. Slip Op. 32372(U), at *5-6, citing CPLR § 4547. This rule is substantively identical to F.R.E. 408(a); both rules prohibit the admission into evidence of statements made in compromise negotiations to prove liability.

¹⁹ *Id.* at *6.

²⁰ 223 A.D.2d 459 (App. Div. 1st Dept. 1996).

²¹ See, e.g., *Lipsky v. Commonwealth United Corp.*, 551 F.2d 887, 893-4 (2d Cir. 1976).

²² Pleas of nolo contendere are inadmissible in subsequent civil or criminal litigation against the defendant who made the plea. F.R.E. 410.

²³ *Lipsky*, 551 F.2d at 893-4.

²⁴ See Sue Reisinger, *Prosecution Agreements, Complete With Denials*, Nat'l L. J., Corp. Counsel (Jan. 7, 2008). Four companies, Zimmer Holdings, Inc., DePuy Orthopaedics Inc., Biomet Inc., and Smith & Nephew PLC, entered into DPAs containing extensive monitorship and compliance requirements; Stryker Orthopaedics entered into a comparatively less demanding NPA. Each company also entered into civil settlement agreements with the DOJ and the Department of Health & Human Services under which they paid millions in fines. According to Reisinger, no prior federal DPAs or NPAs allowed the defendants to deny wrongdoing.

²⁵ See Non-Prosecution Agreement between Alpha Natural Resources, Inc. and the U.S. Attorney's Office for the Southern District of West Virginia (Dec. 6, 2011), available at http://www.post-gazette.com/pg/pdf/201112/alpha_agreement_2_.pdf. The NPA states that it is based on Alpha's recent acquisition of Massey, its extensive cooperation with the government, its agreement to extensive remedial measures and various financial commitments, including restitution to the victims' families.

²⁶ See Philip Shenon, *Ashcroft Deal Brings Scrutiny in Justice Dept.*, N.Y. Times (Jan. 10, 2008); David M. Uhlmann, *For 29 Dead Miners, No Justice*, N.Y. Times (Dec. 9, 2011).

²⁷ See, e.g., *SEC v. Citigroup Global Markets*, No. 11-CV-07387, 2011 BL 307391 (S.D.N.Y. Nov. 28, 2011) (rejecting as against the public interest a proposed consent order between Citigroup and the SEC that would allow Citigroup to dispute the facts of the case in other litigation); *SEC v. Bank of America*, 653 F. Supp. 2d 507 (S.D.N.Y. 2009) (holding that the proposed consent judgment was neither "fair, nor reasonable, nor adequate" because the financial burden would fall on the bank's shareholders, the victims of the alleged fraud).