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WHITE-COLLAR CRIME

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Issues Raised When Rare Techniques Are Used by Prosecutors

The reaction to the highly publicized spate of disclosures of alleged corporate wrongdoing has resulted in a prosecutorial crackdown employing concepts and procedures rarely seen in corporate criminal cases.

Thus, rapid arrests based upon complaints have substituted for thorough, painstaking, more gradual grand jury investigations. Perp walks have been featured over voluntary surrender. Prosecution of corporate entities, with seeming disregard for the innocent workers who join the unemployed, appear to be more permissible. National press conferences to announce local prosecutions are in vogue with an accompanying media frenzy. And, the humiliation of corporate executives by compelling them to assert their constitutional rights on television, has become commonplace.

Such is the response of a law enforcement establishment, driven, in part, by political considerations, to meet the challenges posed by the unfolding series of financial fraud cases.

This article attempts to define and discuss many of the common issues raised in these types of cases.

The Attorney-Client Privilege

Discovery by a corporation of abuse of its

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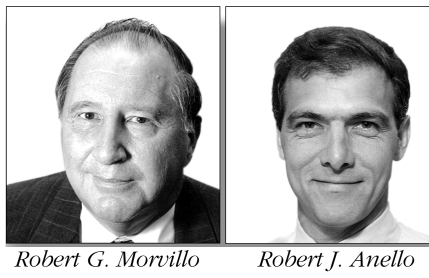

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processes and/or assets often impels a rush to conduct an internal investigation. While this tried-and-true reaction is laudable and encouraged by regulators, it should be kept in mind that an internal investigation can provide regulators, prosecutors and potential plaintiffs with a road map of the wrongdoing. As the name of the game in corporate investigations has become cooperation by the corporation involved, the Department of Justice as well as other regulators such as the SEC, encourage production of the results of the internal investigation, including privileged communications. Prosecutors and regulators claim to weigh heavily a corporation's response to requests for such materials in deciding whether to bring charges against the company itself or to proceed only against individuals.[1] It is now common for the government to ask that the attorney-client privilege be waived and to demand access to interview notes and other work-product.

As a result, some defense counsel are cautioning their corporate clients to eliminate or constrict internal investigations and to avoid reducing damaging information to writing, when feasible. Production of the internal investigation and its product to prosecutors and/or regulators often has adverse repercussions in a civil context.

In In re Steinhardt Partners, L.P.,[2] the Second Circuit found that a party's submission of materials from its internal investigation to the SEC waived work-product protection with respect to all other parties. The court noted that corporations have strong incentives to disclose information to the government, including the opportunity to narrow and shorten an investigation or obtain leniency, and that these incentives exist regardless of whether third parties will also have access to the information. Significantly, the court suggested that where the government expressly agrees to maintain the confidentiality of the disclosed materials, the waiver might not extend to private litigants. Sometimes prosecutors can be convinced to accept the materials with an understanding that they will be treated as confidential.

Southern District Judge Richard Owen recently relied on just such a confidentiality agreement to deny private plaintiffs' motion to compel production of documents from defendant's internal investigation, notwithstanding the fact that the defendant had provided information from that investigation to the government. The defendant in Maruzen Co. v. HSBC USA, Inc. et al.,[3] had an oral agreement from the prosecutor to maintain the materials in confidence and not to disclose their contents to any parties outside the government except as required by law. Judge Owen held that this express confidentiality agreement was sufficient to retain the defendant's claim of privilege with respect to its

internal investigation, and denied the motion to compel.

The possibility that the corporation will waive its privilege compels counsel conducting the investigation to warn those being interviewed that they represent the corporation only and the privilege belongs solely to the corporation.[4]

'Kovel' Protection

With the growth of the complexity of corporate business, attorneys rely on a host of technical experts to help in understanding the nature and import of the challenged activity. Depending on the precise nature of the expert's role, communications to and from that individual should be protected with a written Kovel agreement. In United States v. Kovel,[5] the Second Circuit recognized that where an expert, such as an accountant, functions to help an attorney to consult more effectively with the client, the attorney-client privilege is maintained between the attorney and the expert and also the expert and the client. The concept has been thought to cover a wide variety of experts retained by counsel to assist in understanding the client's position in criminal cases.

In United States v. Ackert,[6] the Second Circuit interpreted and somewhat limited Kovel, stating "a communication between an attorney and a third party does not become shielded by the attorney-client privilege solely because the communication proves important to the attorney's ability to represent the client." In that case, the Court of Appeals found that communications between a company's in-house counsel and an investment adviser for the purposes of clarifying details and tax consequences of a proposed transaction were not privileged. Noting that the purpose of the privilege is to encourage clients to be forthcoming with their attorneys, the court stressed that the privilege protects communications between the attorney and the client, and not those communications that prove important to an attorney's legal advice to the client.[7] Work product protection also may be available to shield some communications with consultants.[8]

Conflicts, Corporate Workers

Corporate investigations, whether internal or external, often pose vexing problems for the corporation's dealings with its employees. It is almost always in the corporation's interest that its employees be represented by counsel. When numerous employees are involved or have pertinent information, expense and potential conflict of interest issues arise. Exchanges of information then become harder to protect, a problem frequently resolved by joint defense agreements. Some corporations are shy about sharing information with their employees in this manner as it gives the employee a potential hold on the dissemination of the information. They also understand that joint defense agreements are frowned upon by some prosecutors.

Employee representation frequently raises issues regarding payment of legal fees. Prosecutors always are alert to potential fact distortion when a witness' legal fees are being paid by a subject of the investigation. However, corporate by-laws as well as state statutes[9] often require corporations to indemnify and advance legal fees to employees.

Prosecutors often become unhappy upon provision of legal fees to employees who may be implicated in corporate wrongdoing. In its guidelines for the prosecution of corporations, the Department of Justice specifically lists a corporation's advancing of legal fees as one sign of a "promise of support to culpable employees and agents," that the prosecutor may weigh in evaluating the extent and value of a corporation's cooperation.[10] Although this appears to ignore the mandatory aspects of indemnification as well as the presumption of innocence, this attitude creates pressure on corporations to abandon commitments to its work force to avoid being penalized.

Another manifestation of prosecutorial attitudes unique to corporate criminal investigations is pressure exerted to fire employees who do not fully cooperate with government investigators. A private employer may terminate an employee who refuses to cooperate with its own internal investigation.[11] Moreover, a private organization, even if it intends to share the fruits of its investigation with law enforcement, is not constrained by the Fifth Amendment in using economic pressure to extract incriminating statements.[12] But the government may not do so.

In a pair of cases decided in 1967, the Supreme Court found that the state may not use economic coercion to obtain incriminating statements. In Garrity v. New Jersey,[13] it held that the state had used unconstitutionally coercive means to obtain statements from police officers who were threatened with the loss of their jobs unless they waived their Fifth Amendment privilege against self-incrimination, and in Spevack v. Klein[14] it held that the state could not threaten to disbar an attorney for refusal to provide incriminating statements and documents. Although some authority suggests that economic coercion induced by the government through a private employer "acting as an agent for the police" can be constitutionally significant,[15] such a proposition does not seem to have deterred prosecutors from assessing a corporation's cooperation negatively for failing to respond when its employees act in a constitutionally protected manner.

Retention and Production

• Document Retention Obligations. Whatever degree of cooperation a corporation decides is in its best interest, it must vigilantly guard against incurring further potential liability arising from its document retention obligations. The demise of Arthur Andersen provides an all too graphic illustration of the need to disseminate timely, clear and effective instructions regarding preservation of possibly relevant materials. It also serves as a reminder that even where the government is unable to bring a complex business or accounting fraud prosecution, obstruction of a criminal investigation, in and of itself, can be ruinous to even the largest company.

The penalties for obstruction of justice have increased since the Andersen prosecution. The Corporate Fraud Accountability section of the recently enacted Sarbanes-

Oxley Act[16] contains an express provision criminalizing tampering with a record or otherwise impeding an official proceeding. That provision amends the criminal witness tampering law to include sanctions of up to 20 years in prison for anyone who "alters, destroys, mutilates or conceals a record, document, or other object, or attempts to do so, with the intent to impair the object's integrity or availability for use in an official proceeding."[17]

Records housed on computers have become extremely useful to prosecutors. Some form of corporate screening may be advisable. These records often are retrievable even if the hard copy has been lost or destroyed. Moreover, corporate employees' e-mails frequently contain unfettered and unguarded communications similar to those overheard on legal wire tap recordings. Indeed, because unlike taped conversations, they are devoid of intonation, humor and facetiousness are not always apparent. Such communications, of course, are a must to recapture in any internal investigation.

Document Production

One concern that arises when a corporation or its employees are called upon to produce documents is how to distinguish between corporate documents and the personal documents of corporate employees. Although the Fifth Amendment does not shield the contents of voluntarily created, incriminating documents, an individual may invoke the Fifth Amendment where the act of producing the document is itself incriminating.[18] That privilege is not available to a corporation, however, and to the extent a corporate employee is acting as a custodian of corporate documents, the employee cannot invoke the Fifth Amendment, because he or she is deemed to be acting in a representative rather than a personal capacity.[19]

However, in instances when personal documents are kept on corporate premises, the act of production doctrine might apply. In In re Grand Jury Subpoena Duces Tecum Dated April 23, 1981,[20] the Second Circuit identified a number of "nonexhaustive criteria" to be evaluated in determining whether a subpoena calls for the production of personal material, for which the employee would be allowed to claim the act of production privilege, or corporate documents, for which no privilege is available. Those criteria include consideration of who prepared the document; the nature of its contents, its purpose or use; in whose possession it was maintained and who had access to it; whether the corporation required its preparation; and whether the document's existence was necessary to the conduct of the corporation's business. Where an individual commingles his or her personal information with corporate material, such as in a rolodex or calendar that contains business as well as personal information, at least one court has held that the "non business material becomes part of the corporate documents."[21]

"The demise of Arthur Andersen provides an all too graphic illustration of the need to disseminate timely, clear and effective instructions regarding preservation of possibly relevant materials."

Conclusion

The above represents but a few of the most frequently faced issues in a corporate criminal investigation. As each scandal rears its ugly head, legislators and prosecutors add weapons weakening the tactical response of the defense. The practitioner constantly must adjust to these changes by understanding the trends and tactics and being prepared to cope with them. It is hoped that interested bar associations will weigh in against practices that demean and are not designed to ensure a just result.

(1) Securities and Exchange Act Release No. 44969, Oct. 23, 2001.

(2) 9 F.3d 230 (2d Cir. 1993).

(3) Nos. 00 Civ. 1079; 00 Civ. 1512, 2002 WL 1628782 (S.D.N.Y. July 23, 2002).

(4) See In re Grand Jury Subpoena Duces Tecum dated July 6, 1987, No. M11-189 (S.D.N.Y. 1987) (Keenan, J.).

(5) 296 F.2d 918 (2d Cir. 1961)(Friendly, J.).

(6) 169 F.3d 136 (2d Cir. 1999).

(7) See also SR Int'l Business Ins. Co v. World Trade Center Properties, LLC, et al., No. 01 Civ. 9291, 2002 WL 1334821 (S.D.N.Y. June 19, 2002); 2002 WL 1455346 (S.D.N.Y. July 3, 2002) (denying Kovel protection to insurance advisors and observing that "[n]othing in the policy of the privilege suggests that … attorneys, simply by placing accountants, scientists or investigators on their payrolls … should be able to invest all communications by clients with such persons with a privilege the law has not seen fit to extend when the latter are operating under their own steam.")(quoting In re Grand Jury Matter, 147 F.R.D. 82 (E.D. Pa. 1992); Calvin Klein Trademark Trust v. Wachner, 198 F.R.D. 53 (S.D.N.Y. 2000). But see In re Copper Market Antitrust Litigation, 200 F.R.D. 213 (S.D.N.Y. 2001); FTC v. Glaxo SmithKline, 294 F.3d 141 (D.C. Cir. 2002).

(8) In re Copper Market, supra.

(9) See e.g., N.Y. Bus. Corp. Law §722; Del. Gen. Corp. Law §145.

(10) Federal Prosecution of Corporations, attached to Memorandum of Deputy Attorney General Eric Holder, June 16, 1999.

(11) See Nuzzo v. Northwest Airlines, 887 F. Supp. 28 (D. Mass. 1995)

(12) See United States v. Solomon, 509 F.2d 863 (2d Cir. 1975) (No Fifth Amendment violation where New York Stock Exchange threatened to expel defendant unless he submitted to interrogation, and defendant was later indicted and convicted on basis of those statements).

(13) 385 US 493 (1967).

(14) 385 US 511 (1967).

(15) United States ex rel. Sanney v. Montayne, 500 F.2d 411 (2d Cir. 1974).

(16) Sarbanes-Oxley Act of 2002, H.R. 3763, 107th Cong. §307 (2002).

(17) Previously, document destruction was prosecuted under the general obstruction of justice statutes, and was punishable by up to 10 years in prison.

(18) See, e.g., In re Grand Jury Subpoena Duces Tecum dated Oct. 29, 1992, 1 F3d 87 (2d Cir. 1993), cert. denied, 510 US 1091 (1994).

(19) See Braswell v. United States, 487 US 99 (1988). Former employees may assert the Fifth Amendment privilege when the act of producing corporate documents in their possession is incriminating because they are no longer acting as the corporation's agent. In re Three Grand Jury Subpoenas Duces Tecum Dated January 29, 1999, 191 F3d 173 (2d Cir. 1999).

(20) 657 F2d 5 (2d Cir. 1981).

(21) In re Grand Jury Subpeona Duces Tecum dated January 30, 1992, 804 F. Supp. 582 (S.D.N.Y. 1992).

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