

ROUNDTABLE

White-Collar Defense

EXECUTIVE SUMMARY

Today's headlines are filled with white-collar crime prosecutions. This is due to a number of factors, including the mortgage scandal, heightened scrutiny of corporations from the Department of Justice (DOJ) and the Securities and Exchange Commission (SEC), and increased enforcement of the Foreign Corrupt Practices Act (FCPA (15 U.S.C. §§78dd-1-78ff)). In September, for example, a married couple of film executives was convicted (in *United States v. Green*, No. CR 08-59 (C.D. Cal., jury verdict filed Sept. 11, 2009)) of bribing a Thai official in order to obtain lucrative contracts for an international film festival. A July conviction in *United States v. Bourke* (No. 05-518, (S.D.N.Y. jury verdict filed July 10, 2009)) involved FCPA violations in Azerbaijan.

Our panel of experts discusses these cases along with other topics such as the honest-services (18 U.S.C. 1346) cases currently before the Supreme Court: *Black v. United States* (530 F.3d 596 (7th Cir. 2008) cert. granted, 129 S. Ct. 2379 (2009)); *Weyhrauch v. United States* (548 F.3d 1237 (9th Cir. 2008) cert. granted, 129 S. Ct. 2863 (2009)); and *Skilling v. United States* cert. granted (554 F.3d. 529 (5th Cir. 2009) cert. granted, 130 S. Ct. 393 (2009)). The panel includes Michael Farhang and Debra Wong Yang of Gibson, Dunn & Crutcher; Carolyn Kubota of O'Melveny & Myers; and McGregor "Greg" Scott of Orrick, Herrington & Sutcliffe. *California Lawyer* moderated the roundtable, which was reported by Krishanna DeRita of Barkley Court Reporters.

MODERATOR: What impact we are going to see or are we already seeing from the Greens' conviction? What does it mean for your work?

YANG: The interesting thing about the *Green* case is the fact that it was done in conjunction with a number of foreign investigative offices, which I think is a common trend that we are starting to see.

KUBOTA: The *Green* case is noteworthy because the DOJ worked with one of the regional U.S. Attorney Offices. Word in the defense community is that there are now agents based in Los Angeles who are dedi-

FARHANG: In the *Bourke* case what you had was accountability of the defendant for a third party's actions. One of the things the government alleged was that the defendant knew about payments being made by this third party. What it points to is the importance of conducting due diligence on third parties, so you don't find yourself at risk for actions of a business consultant.

YANG: It broadens the circle of what it is that you are liable for. After *Bourke*, you can't have willful avoidance and willful blindness. You actually have to take the affirmative steps. A lot of companies in the

est. It really is driving home the point that you need to have a blue-chip compliance program. So companies that have an existing compliance program, still need to go back through it and make sure there are no gaps, that it's up to date, that you are doing the right kind of auditing.

SCOTT: The prosecution of individuals as opposed to corporations will lend itself to more prosecutions, [rather than] deferred prosecution agreements (DPAs). It's going to be very difficult to have DPAs with individuals as opposed to entities. So if this is a new area of emphasis and focus, then we are going to see more actual indictments. Then the two cases are very interesting because it shows the geographic reach of the jurisdiction. The Department is touching all over the world on this issue.

FARHANG: In two recent speeches, the new assistant attorney general cited the *Green* case and noted that since 2005, the DOJ has actually brought 57 FCPA cases—which is more than the total number of cases that they brought since the inception of the FCPA up until 2005. So the enforcement has exploded over the last few years and shows no sign of abating. The FBI now has specific squads tasked with the FCPA enforcement.

MODERATOR: Does the *Green* conviction signal

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cated to FCPA. Those developments could lead to more prosecutions coming out of this district. The other thing that's noteworthy about *Green* is that it involved a prosecution of individuals. That is somewhat of a departure from the practice in prior cases. It's another shift that could manifest itself in future cases.

past thought that because they had engaged in joint ventures or because they were minority shareholders, that gave them protection. That's not the case any more. You are still responsible and going to be held responsible for doing that due diligence into third parties, even if you are not the majority inter-

that entertainment companies in particular are now going to be a FCPA target?

YANG: It's more of a signal that if you are a company that's involved in businesses in far flung places of the globe, or in some of these countries that have a particularly bad transparency record, then you are going to be part of a focus. As an American company, if you are trying to conduct business in a foreign country that is used to a completely different way of culture, you have to approach that minefield very carefully.

KUBOTA: The DOJ has shown in other areas (like medical devices and the oil-services industry) that when it does a case in a particular industry, it takes its knowledge about practices in that industry and uses it to pursue other cases.

MODERATOR: In the '90s, white-collar defense was dominated by boutique firms. But in the last few years, the white-collar defense bar has shifted to international firms. Is this because of increased FCPA enforcement or are there other reasons for that?

FARHANG: Some of the things that happened in the past 10 years were Enron, Sarbanes-Oxley (Pub. L. 107-204 (2002)), and a series of significant cases in the financial area involving large companies. As most practitioners have seen, companies undergoing DOJ and SEC scrutiny need assistance with conducting internal investigations, responding to government investigations, and regulatory inquiries and requests. But they may also have securities litigation that will crop up. They could have qui tam cases come up. They need both civil litigation and criminal white-collar expertise; they need counseling regarding their disclosure obligations. What they need, essentially, are the resources of an international firm that is going to be able to provide advice on a number of different levels. That is the type of scenario that may favor large international firms over smaller boutiques.

SCOTT: It's certainly helpful when you've got an American-based corporation that has affiliates in foreign countries and all of a sudden there's a problem. The ability of an international firm is to reach out to partners in China, in Russia and to fill in the blanks and get very quick turn around on what is the law is there, with respect to A, B and C—in a very real-time way so that corporations can make the right decisions in a

timely way and deal with issues as they arise.

YANG: Companies have gotten bigger. They just keep growing and buying up other smaller companies, and we are just starting to see larger and larger companies that have a much more global sort of extension than previously. The regulators generally follow the business. For example, pharmaceutical companies that manufacture and sell in other foreign countries are always going to be under scrutiny by Health and

reflect different issues. With *Skilling* and *Black*, it's the fundamental question of whether this statute may be used in the private context or is it only for public officials? Clearly it's been used for private conduct, but I'm not going to be surprised at all if the Supreme Court circumscribes that because it is such a vague standard. If you look at the *Skilling* case, they were lying about the assets of the corporation. But if the net result was to at least in the short term maintain the viability of the corporation,

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—Michael Farhang

Human Services, the SEC, or the Department of Justice. The company is not being examined merely for FCPA violations, but the FCPA charges allow prosecutors and regulators one way to determine if the company is violating in a foreign country.

KUBOTA: I don't think that the shift in white-collar practice from boutiques to international firms really has much to do with FCPA. Most of white-collar work doesn't have anything to do with it. It's just one area in which white-collar practitioners work. Big firms recognized that white collar was a growing area. It's an area where cases are often highly leveraged and profitable and that was the impetus to move into the white-collar area.

MODERATOR: Let's talk about *Black v. United States* and *Weyhrauch v. United States*. Will these cases give the Court the opportunity to provide guidance on how the honest-services fraud statute can be used in both a public and private context?

KUBOTA: The *Skilling* case is also before the Supreme Court and it also has an honest-services issue. So, that's actually three cases the Supreme Court has taken up. I think it's clouding up to storm. The Supreme Court clearly feels like more guidance is required, but I don't think they can just say there has to be an identifiable monetary harm. They already went down that road in *McNally* (*McNally v. United States*, 483 U.S. 350 (1987)) and Congress answered with the honest-services provision. So it's going to have to be something different than that.

SCOTT: The three cases in combination really

is that a violation of the honest-services statute? And then once you move away from private citizens as opposed to public officials, the *Weyhrauch* case out of Alaska is really interesting because you have a state legislator who, from all reports, did not violate any state reporting or legal requirements, but yet has now been charged in federal court with violation of honest services. If he's not violated any of his duties as a state legislator, it's going to be pretty difficult to turn around and say he's violated honest services at the federal level. If I were to hazard a guess, they are going to severely curtail this, putting it back on Congress to come up with a far more circumscribed statute to set out clear boundaries of what can be properly brought under the statute.

MODERATOR: Does the honest-services fraud statute give prosecutors too much leeway?

KUBOTA: There can't be any dispute that the terms of the statute are ambiguous. That's also evidenced by the fact that there's a circuit split on the meaning of the honest-services provision. But this is a controversy that's been going on since the beginning of the mail-fraud statute—it's a broadly worded federal statute that can be adjusted to fit almost any fact pattern.

SCOTT: As U.S. attorney, we brought some cases against public officials on honest services, and it serves a true purpose. In many of these circumstances you have public officials who are playing fast and loose, and you don't have a more clearly defined, articulated statute that fits the conduct. We

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have a right to expect that our public officials act with integrity and honor in conducting their public business. And the statute—while it probably does need to be tailored back—does provide a real tool for prosecutors in appropriate circumstances.

MODERATOR: What should we be concluding from the reversal of the conviction of the former Brocade CEO Greg Reyes, in *United States v. Reyes* (577 F.3d 1069 (9th Cir. 2009))?

YANG: The issue of prosecutorial misconduct is nothing new. It's just that these days it has a bit more audience than it has in the past. People who are raising that as a defense are sophisticated and understand all the rules that a prosecutor has to live by in putting their case together. If you are advocating for the prosecution, you've got to watch it and you've got to make sure that you are not right on the ethical line, but well above the line. Now the onus is on the prosecutors to try their case knowing that a court or defense counsel may raise the issue later.

FARHANG: It points up the general understanding or rule that the government is held to a higher standard in cases because of its obligation to not just prosecute but also to do justice. In that case, the circuit felt that the government had gone too far. It's difficult to say that the lesson necessarily carries results for other stock-option back-dating prosecutions.

SCOTT: Attorney General Holder's decision to dismiss the Stevens case certainly—in terms of the people that I've spoken to—sent a shudder through the Department. There is a sense that he did not articulate to the field why he had done what he had done, and that there was a sense of that he—and again, I'm relating conversations I've had with line prosecutors—had overreacted to the circumstances and did not adequately convey to his troops why he did what he did. That causes folks to get a little gun shy, appropriately if they are overstepping that line that's been described. But if you look back statistically at the Department over the past several years, the findings of prosecutorial misconduct have not increased. The allegations have, but the findings have not, and we on the defense side need to make sure that we are not the little boy who cried wolf where we are alleging prosecutorial misconduct in every case because it's the fashionable thing to do right now.

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MODERATOR: Has the ongoing Broadcom trial (*United States v. Ruehle*, No. SACR 08-139 (C.D. Cal. Jury voir dire commenced Oct. 22, 2009)) had any impact on your business?

KUBOTA: There has been a discernible up-tick in sentiment among potential jury pools, a sensitivity to corporate greed. All of these cases have served to underscore the theme that companies are bad, corporate greed is evil, et cetera. As a result, there is increased resentment of corporations, corporate executives, and the perception of fat cats raking in money. That can go well beyond cases like *Reyes*, and percolate down to more conventional cases involving corporate defendants.

FARHANG: Stock option backdating cases and other cases in the accounting-fraud area highlight the challenges that the government faces to prove and make facts simple and understandable for juries. The average juror is probably not going to have the type of accounting expertise for issues like these. But these are issues that have to be gone over in great detail during those trials and prosecutors are going to tell juries that “This is a simple case about lying, deception, greed,” and defense attorneys will try to argue that “This is a complicated case about accounting.” So it highlights that you have to be able to synthesize, as the prosecutor in a trial, very complex transactions and situations for a jury so they can boil the evidence down to the core issues.

YANG: From the jury’s perspective, you don’t see this kind of lifestyle very often. There’s something fascinating about it and there’s also something appalling about it. They are not used to the kind of money that’s made, the lifestyle that people have, and those items on a certain level makes it very difficult if you are defending that person because you are constantly having to play down aspects of just how someone at that level with that kind of income lives their everyday, ordinary life.

SCOTT: With some exceptions, corporations, directors, and officers have essentially dealt in anonymity with the public at large in conducting their business. When the bailout occurred and the pinnacles of the American financial structure accepted hundreds of millions of dollars from the government, the taxpayers now care because it’s their money.

MODERATOR: Everybody is in trouble over mort-

gages, lawyers included. Five municipalities within California’s Eastern District are just a hotbed of mortgage fraud. Is this situation unprecedented?

KUBOTA: What’s past is prologue. This feels pretty familiar to the savings and loan crisis in the late ’80s and early ’90s. What’s different this time is there’s been larger degree of securitization of mortgages—pooling and selling them in the secondary market. Even in the savings and loan crisis, a

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lot of lawyers and auditors were sued in connection with their representations in loan transactions, or in connection with their work for the savings and loans themselves.

YANG: The only difference this time around is that you’ve got other people who are on the hook for it: All the investment houses, all the people who put portfolios together and made representations about the loans, all those who audited those portfolios, and all those who marketed those funds. My general impression in California is that it’s not going to let up. In speaking to some of the current candidates for attorney general, some of them have said that it is one of their top priorities. There’s a perception that that wrong has not been completely righted here in the state. So there’s going to be a focus from the AG’s office too.

SCOTT: One of the things that people don’t fully grasp is that the mortgage fraud crisis was not this one type of fraud for a specific amount of time. It’s a morphing, rolling phenomenon and you had all the things going on in the early 2000s up to 2005, with no income, the fixing of loan applications, all those things. Then it morphed into foreclosure fraud. Then it morphed into builder buy-out fraud. So it’s not done. I don’t think we are anywhere near the end of this thing and home prices have not really come back in California. There’s a glut of houses that are still in foreclosure on the market. So this is something we are going to be living with for a long time to come. One thing I would point out that is different from the savings and loan crisis, is there has not been a coordinated national response from DOJ on

this issue. It’s been left to the individual U.S. attorneys to sort it out. It’s just now that they are rolling out assistant U.S. attorney positions devoted to mortgage fraud. The horse has left the barn a little bit. There really was no focused concentration earlier on at a national level on this issue. So certain U.S. attorneys had to deal with it individually.

FARHANG: Most of us have been waiting to see those very large prosecutions in this area. Part of

the problem could be perhaps a lack of coordination in these cases—but also just the difficulty of structuring a case in an environment where the market reaction in the housing industry and mortgage industry took everyone by surprise. Effectively you are going to be trying to prove that the executives at some of these companies had knowledge that the market—including the sophisticated investors and underwriters—did not have at the time. It’s going to be very difficult in some ways for the government to reconstruct that knowledge. This may be part of the reason the government is taking time on the cases, because if they bring one, they want to make sure they get it right.

SCOTT: The classic defendant we had when I was U.S. attorney was a broker or loan officer, because you are going to be able to prove that lie on a document for a loan application more readily. This Bear Stearns verdict that came down in the last couple of weeks (*United States v. Cioffi*, CR-08-415 (judgment of acquittal filed Nov. 16, 2009)), that really was the flagship case for the Department because they had these “smoking gun” e-mails. And they got a “not guilty” verdict. That verdict further makes the point that it’s going to be very difficult to prove these cases at a higher level in the financial food chain than with a loan originator, the mortgage broker, or the loan officer. And the Department is going to have to take a step back after the Bear Stearns and try to develop a better strategy.

MODERATOR: What went wrong in that case?

SCOTT: There were some very inflammatory e-mails

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exchanged between a couple of executives, but the defense was able to very successfully convey to the jury that the prosecution had taken those e-mails out of context. It shows quite well that as prosecutors, you get real excited about e-mails. It's right there. You can see it, but there has to be context.

MODERATOR: Is it true that a lot of companies voluntarily disclose FCPA violations to the SEC?

KUBOTA: Yes. Where companies find a widespread or systemic problem, or a single incident that's very serious, then I would say, yes. If they find an isolated incident—not necessarily. But in serious cases where they realize that the consequences are going to be terrible if they don't report it and the government finds out about it, I would say yes.

YANG: If you look at some of the cases where companies have self-disclosed, I don't think many of them have gotten off scot-free. All of them have had some sort of penalty imposed on them. It's difficult to know what the underlying value of the corrupt act is, or how much the ill gotten gains were. Therefore it is hard to measure whether the penalty is a lot in comparison with the wrong or not. But

what does it look like today? That's a fluid thing that literally changes from week to week for some companies.

FARHANG: Another consideration for any company in that position is really how are they going to make the best case to the government that this is an isolated event? That it's not representative of the way the company does business and it doesn't implicate the integrity of management. One of the questions a company will be asked upon making a disclosure like this is what was your compliance program before this happened? Had you instituted a system of training, a system of reporting, adequate system of controls, were you conducting due diligence on third parties? If a company can't answer those questions, either way it is not going to look favorable to the government. Companies, even before they identify a problem, need to make sure that their house is in order from a compliance perspective so when that problem does crop up later, they are going to be able to make the best case they can that the company is not at fault even if individuals can be at fault.

MODERATOR: If your corporate clients self-disclose and still get pretty harsh penalties, isn't that mak-

ing people hesitant to self-disclose and hope that it doesn't get found out?

YANG: Some of those blue chip companies that do conduct very stellar compliance practices still run into problems because they purchase companies in other locations and those companies have a completely different kind of history, personality, and compliance program. So what's really important when you are trying to determine whether or not to self-disclose, is to have a complete and comprehensive internal investigation. You are not going to want to step up to the government and tell them, "Hey, I did something wrong," until you know exactly what it is that you've done. It may be that it came out of a smaller company or it may be your operations in a foreign country that you may not have as much daily control over. That's why the notion of internal investigations in the context of FCPA is vitally important these days. You can't even begin to make a good assessment of self-disclosure unless you have that information available to you.

KUBOTA: A complete internal investigation is step one because that's the only way that you can really measure the upside and downside of self-disclosure. Once the government is involved, you are not going to be able to control what they investigate. So you really need to know: If the government gets in and does an exhaustive investigation—what's the downside?

MODERATOR: So once you have made the internal investigation, what's the tipping point? What is it that's going to make a difference?

KUBOTA: There are a lot of factors. Is this an area where the DOJ has already been actively investigating? What's the probability that they would stumble upon this on their own? Ultimately—if you don't self-disclose—you are gambling on the probability of the government not finding it.

FARHANG: Companies that are responsibly handling allegations of misconduct and conducting exhaustive internal investigations are almost making the choice at the outset. A company is not going to want to create a record of an investigation and then risk not disclosing it. There are a number of different ways the government can learn about issues. They can learn about them from a whistleblower, a dis-

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they are coming out with a number of disclosures where the penalties are in the \$5 million up to \$20 million dollar range. [The DOJ's Deputy Chief of the Fraud Section] Mark Mendelsohn said at open conference that if it's a situation where you have one low level person with an improper contract that was entered into, then he's not really that interested in it. But if it's a high-level person, he's interested in it and he expects that the company will look at every single contract that the person has touched. Part of when you determine whether or not to self-disclose, is assessing and weighing what is it that you have done once you discovered wrongdoing. How have you remediated? What is the depth of the harm and

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grunted employee, a competitor, other third parties that may be involved in the transaction, and so on.

KUBOTA: I agree: If you create that kind of record and don't self-disclose, you've put yourself in the worst possible situation if the government finds out.

FARHANG: The DOJ has shown interest in allowing companies to self-rehabilitate even where they have made voluntary disclosures. The DOJ is using the carrot-and-stick approach by allowing the company to rehabilitate itself even in a case of serious misconduct.

YANG: The government actually doesn't have unlimited resources. So they really do pick and choose who they want to go after. If it appears that a company is engaging in actions that are remediating the problem, then there's less incentive for them to get involved because other companies aren't making the same effort. So by going through all that and doing all the right things after the internal investigation and starting to put things together and make them all up-to-date, it provides less incentive for the government to come in and want to take a strong hand in what it is that's going on.

MODERATOR: Does the DOJ's heightened attention to white-collar crime mean that firms like yours are banking on a business boom in the form of internal corporate investigations?

YANG: I don't know what's going to happen in the future, but I will say unlike other practice areas that have had more of a roller coaster ride in the past two years—in the white-collar world, my general perception is that it's stayed relatively stable.

KUBOTA: It ties into some things that Michael [Farhang] was saying earlier about how criminal prosecutions of corporations have really changed in the past ten years. Indictments have, probably with a lot of justification, come to be seen as the death knell for companies. It also grows out of the Thompson memos—which of course are no more—but their legacy lives on. There's a very strong inclination on the part of companies who come under investigation to just staunch the wound immediately, rush to cooperate with the government, get whatever benefits they can get out of cooperating, and distance themselves from any potential individual wrongdoers. That whole phenomenon has really changed the shape of white-collar defense.

FARHANG: Federal acquisition regulations now require companies to have an ethics code, a business-conduct code, and specific internal controls to catch fraud in government contracts. There's now a requirement that companies that learn of violations of federal criminal law in a government contract actually disclose those to the contracting authorities or face debarment, if it's later found that they knew of the misconduct but failed to report it. It's going to change a lot of ways the government looks at these issues.

SCOTT: When we were sitting at our annual partners' meeting in January, we were projecting it was going to be a busy active year because of all the fallout from the financial meltdown. But I don't know that we've seen that to the extent that we had projected. Part of the problem is that everybody thinks DOJ is in Washington. That's the face of the Department, but the reality is that the overwhelming amount of the work done by DOJ is done by the U.S. Attorney offices. And the Obama administration has been slow to fill the U.S. attorney positions. They don't have their leaders deployed to the U.S. Attorney's offices to the extent that they will a year from now or six months from now. DOJ has been slow to address a lot of the white-collar related issues that have

being held to a higher standard. They are going after them as individuals—anyone who is part and parcel of putting the funds together. The other interesting tweak is that judges are getting a bit more selective over what it is that they are going to approve for settlement. Everybody is scrutinizing this so much more and not wanting to let anything go by, and not let any rock that may have funds under it go unturned.

FARHANG: To what extent are the SEC and DOJ effectively deputizing private firms to do their work for them and to what extent can they both get the benefits and avoid the burdens of the investigative work that those firms are doing for them? We have prosecutions within the past few years of executives and companies for making false statements to private-firm lawyers who conducted internal investigations. At what point will the government become accountable for these internal investigations or the way they are done? One of the things that lawyers in our position are confronting right now is understanding where are the limits of the role of internal investigators? Where does the reach of the government end and where does the private realm exist? Government really has expanded its jurisdiction in these cases to reach almost every aspect of the

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come from the financial crisis and otherwise. We are going to see an up-tick in that once more U.S. attorneys are confirmed, once the full leadership is in place back at Justice.

MODERATOR: What impact is this heightened scrutiny of the SEC and the DOJ having on your business?

YANG: What's interesting to me is to see how much more aggressive the SEC is now. In the multitude of ways, some of the SEC receivers are being very broad about what they are going after. So for example, they are not just going after Madoff and retrieving his ill-gotten gains, but the people who helped raise funds for him and in some cases their family members too. You also see them going after people who should have known, and that they are

internal investigation. At some point, courts may push back.

SCOTT: There's a Ninth Circuit case that came down in the past 15 months in which there was, essentially, a parallel SEC and grand jury proceeding and the Ninth Circuit essentially blessed that coordination (*United States v. Stringer*, 521 F.3d 1189 (9th Cir. 2008)). That was a broadening of the door through which investigators could collaborate and work together on these investigations. We'll see more and more of that.

KUBOTA: The SEC has also taken steps to streamline its internal processes. They've reduced the number and level of approvals that are required for different sorts of preliminary steps like issuing subpoenas. I think they are trying to pair down the bureaucracy so that they can be a little bit more agile. ■