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Government's Abuse of Lawsuits

Some people, perhaps many, thought that aggressive governmental prosecutions had turned a page when Eliot Spitzer went from being New York's Attorney General to occupying the governor's chair. Not so. The 800 lb. gorilla named Mr. Spitzer may be gone, but there are many other gorillas that are just as big and just as mean.

Sure, the Justice Department seems to have learned its lesson from the Arthur Andersen mess — why destroy a company by indicting the entity and putting 90,000 people out of work, based upon the acts of a few individuals? Instead, we now have the increasing use of deferred prosecution agreements. These governmental protocols have had their own problems and inconsistencies in application; some would argue abuses — in a case involving Bristol-Meyers Squibb, one of the Justice Department's demands was that the company endow a chair at the New Jersey U.S. Attorney's law school alma mater, Seton Hall University School of Law.

Even with strange governmental conditions like these, companies willingly go along with deferred prosecution agreements. Why? Because if one were forced to choose between a corporate indictment (certain death) and deferred prosecution, that is not a close call.

At the same time, the government has shown no laxity or lack of imagination in going after individual corporate executives. A few examples of these efforts should suffice to scare just about anyone.

The KPMG litigation before Judge Lewis Kaplan in the Southern District of New York is certainly a good case in point. There, the accounting firm's efforts to avoid corporate indictment included waiving every privilege it could

think of and also deciding to forego the advancing of attorneys' fees for numerous KPMG partners, already being criminally prosecuted by the Justice Department. In other words, the firm agreed to cut them loose without any financial assistance. When that latter decision was challenged by the affected individuals on the ground that denying attorneys' fees meant they could not put up an effective defense, Judge Kaplan ruled that the individuals' Sixth Amendment right to counsel had been violated by the prosecutors' pressure on KPMG to cut off fee payments.

Judge Kaplan subsequently dismissed a number of the indictments on the same Sixth Amendment grounds. That dismissal is now up on appeal to the U.S. Court of Appeals for the Second Circuit. Unfortunately, Judge Kaplan may well be reversed. Why? The Justice Department's strong-arm approach may be a wrong without a remedy. This is because KPMG, a private partnership, is not a public company, has no corporate by-laws, and is not formed or incorporated in Delaware and thus not governed by Delaware law, which specifically provides for the advancement of attorneys' fees.

Another example of take-no-prisoner tactics by the Justice Department involves Chiquita Brands International, which found itself in the no-win situation of paying extortion to a Colombian paramilitary organization that is listed by the State Department as a terrorist body so that employees of Chiquita's Colombian subsidiary would not be kidnapped or killed. When senior executives and outside directors learned of the State Department's designation, which makes such payments a federal crime, they decided to "self-report" to the Justice De-

partment and seek guidance on what to do going forward.

The government has been encouraging "self-reporting" for years, citing it as a best practice in corporate governance. One of the self-reporting outside directors of Chiquita was a former head of the Securities and Exchange Commission, Roderick Hills. Department of Justice officials acknowledged to the Chiquita officials that the company was in a "complicated situation," stated the obvious (i.e., that the payments constituted a violation of federal law), but gave no guidance as to what the company should do.

After a number of months went by, with additional payments being made and Chiquita continuing to interface with the government, the Justice Department went into a full-court criminal press against the company that ultimately led to a felony plea by Chiquita and a \$25 million fine.

Not satisfied with that, the Justice Department then publicly threatened to indict the self-reporting Chiquita officials. Only after what appears to have been an intense lobbying effort on behalf of the extraordinarily well-connected Mr. Hills, did the Justice Department recently decide — in its "discretion" — not to indict the individuals. But will the next "self-reporter" who is maybe not as well-connected get the same treatment? Stay tuned.

One particularly Kafkaesque tool the government loves to employ is a whip-saw process known as parallel proceedings. They bring on criminal and civil cases against the same target(s) with prosecutors (i.e., the Justice Department) and regulators (i.e., the SEC). The dynamic this creates is very powerful and hard to defend against. Oregon Fed-

eral Judge Ancer Haggerty pushed back in a recent case, dismissing criminal indictments after finding that the SEC had effectively misled the targeted individuals about its joint efforts with the Justice Department's concurrent criminal probe.

On April 4, 2008, however, the U.S. Court of Appeals for the Ninth Circuit reversed Judge Haggerty's decision on the ground that an SEC document (SEC Form 1662) had been provided to the individuals and their counsel. This multi-page, small type document discloses, among other things, that any information you provide to the SEC "may be used against you in any federal ... civil or criminal proceeding brought by the Commission o[r] any other agency."

According to the Ninth Circuit, this written language made unimportant/irrelevant not only that the Justice Department had scripted the SEC on how to trap the individuals into making false statements that would further a criminal case, but also a misleading answer by an SEC attorney to defense counsel, who specifically asked whether his client was a target of any federal criminal investigation. In short, all is fair in love and war when the government does it.

Other extreme prosecutorial examples by the SEC and the Justice Department abound at poster-child companies such as Enron and General Re, but the foregoing should be sufficient to forewarn, and forearm, any corporate executives skating close to the edge.

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