Criminal Cases

Representing Individual Officers and Directors

by Jack E. Fernandez and Caroline Judge Mehta

Try the following exercise. Imagine a knock at your door at home at 7:30 a.m. The kids are getting dressed for school and you are having coffee with your spouse. You open the door to find two armed federal agents standing in full view of your neighbors with raid jackets that have the letters FBI emblazoned across the back. One of the agents hands you a letter that says, "[y]ou are a target of a grand jury investigation. The agent who handed you this has probable cause to handcuff you and take you to jail. The government is investigating mail fraud allegations that your firm over-billed your clients." Then the agent hands you a grand jury subpoena and asks if you have time for a little chat. You get the idea.

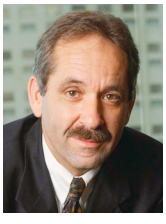
Any corporate employee targeted or charged today for a white collar crime has entered a surreal world fraught with potential for emotional and financial disaster. And let us be clear. We are not talking about a corporate employee caught stealing or embezzling or engaged in some other form of self-dealing. We are talking about corporate employees who never put one penny of ill gotten gains into their pockets but who nonetheless find themselves targets in highly complex, and in many cases untested, "*malum prohibitum*" criminal cases. Often, they will have been "left at the altar" with no assistance (financial or otherwise) from their erstwhile corporate employers on whose behalf they thought they were acting. This is so because of a vast new array of prosecutorial weapons including, among others, the United States Sentencing Guidelines, the Principles of Federal Prosecution of Business Organizations promulgated by the United States Department of Justice (the so-called "Thompson Memorandum"), and the Sarbanes-Oxley Act of 2002, which seeks to improve financial accounting, corporate governance and securities regulation by means of numerous criminal, civil and administrative reforms (including new criminal offenses, amendment of several old ones, and significantly increased sentences for both). *See* S. Salky & A. Rosman, *Is Sarbanes-Oxley Subject to Constitutional Challenge?*, Washington Legal Foundation, September, 2004; S. Salky & A. Rosman, *SOX on Trial: The* Scrushy *Case Tests Sarbanes Oxley's Certification Provisions and Raises the Bar on Causing Others to Falsely Certify*, The Deal, June 6, 2005.

What seems to emerge from recent litigation is that prosecutors, while still pursuing traditional corporate crimes (embezzlement, fraud, illegal pollution, fraudulent financial statements, etc.) have shifted their scrutiny to conduct that is perceived to be against public policy. Many state attorneys general believe that they should focus on whole industries (tobacco, fast food, mutual funds, pharmaceutical) for the risks allegedly posed to the public by these industries' products. Most often, these investigations result in blockbuster civil settlements and integrity agreements, but few indictments. When indictments are returned, under the current criminal regime, they tend to be against individual corporate white collar defendants who are likely to find their corporate employer aligned, with the government, squarely against them.

The Way We Were

That a corporation would, as a matter or course, align with the government and against its employee is a relatively recent phenomenon. In the past, criminal defense counsel for the corporation would quickly investigate the conduct involved and hire competent defense counsel for potential individual corporate targets. Operating pursuant to a joint defense agreement, attorneys for both the corporation and individuals would figure out what happened and begin preparing a defense. While each defense counsel would zealously protect its own client, and often strike the best agreements available with the government, the joint defense agreement lent order and reason to that process. In many cases, counsel for the corporation would take the lead in attempting to strike a global settlement that included non-prosecution of individual targets. (For an excellent description of how the old paradigm worked, *see* Evan Thomas, *The Man to See*, (1992), which describes the life, times and practice of the late Washington D.C. defense attorney, Edward Bennett Williams.)

Certainly, there is much to be commended about this adversarial approach. The government could sometimes be wrong, and sometimes clients, even corporate ones,



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were innocent, and ultimately proven not guilty. The adversarial approach recognized that not every novel theory of prosecution is worthy of indictment, and not every government tactic for obtaining information is legitimate. Many of our civil defense colleagues intrinsically understand this, as they too are called on to defend against state attorney general investigations, with the attendant threat of adverse publicity, civil lawsuits and resultant loss in capital value for their corporate clients who, in general, are engaged in perfectly legal conduct. What better than a vigorous and independent adversary to ensure honesty in such a system?

The Way We Are

Enter the brave new post-Enron world. Today, a corporate attorney operating under the old adversarial paradigm could create massive exposure for the corporation he or she represents. There are two main reasons for this. The first is the United States Sentencing Guidelines, which were amended to create lengthy punishments for corporate wrongdoers but left breathing room for corporations with effective compliance programs that cooperated with the government in ferreting out corporate wrongdoers. *See U.S.S.G.* §§8A, 8B, 8C and 8D. These Guidelines permit an appropriately cooperative corporation, if convicted, to receive a much more lenient sentence.

The second, and probably more significant, factor explaining the death of the old paradigm is the promulgation of the so-called Thompson Memorandum. Authored in 2002 by Deputy Attorney General Larry D. Thompson, *Principles of Federal Prosecution of Business Organization* addresses precisely what behavior a corporation must (or, more importantly, must not) engage in to avoid being charged in the first instance, which is far more important to a corporation than lenient post-conviction treatment. The Thompson Memorandum, which Florida white collar defense attorney Roma Theus calls the "Rosetta stone" of the Department of Justice Manual, encourages corporations to: i) waive applicable privileges; ii) turn over the results of their internal investigations; iii) assist in the prosecution of their employees involved in the allegedly illegal behavior; and iv) refuse to fund those employees' defense. A corporation and its attorneys are now, in every practical effect, government agents. *See* Andrew Longstreth, *Double Agent*, February 2005 American Lawyer (where in the past a lawyer representing a corporation "jousted with the government to limit the flow of information[,] [t]oday,… [h]e (or she) conducts hundreds of interviews, scans company computers for damaging e-mails, rummages through the CFO's wastebasket, and then hands potential evidence over to the government… [which] can form the spine for an indictment." *Id.* Despite countervailing considerations for a corporation, such as the threat of subsequent civil litigation by private litigants, it is now standard for an attorney representing a corporation to advise general counsel to waive the attorney-client privilege.

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As things currently stand, the stakes for a publicly held corporation are simply too high not to cooperate fully. The fate that befell Arthur Andersen served as a cautionary tale to many companies about the cost of doing battle in today's world. Its 2002 indictment and subsequent conviction caused the demise of the 90-year old institution, making the ultimate reversal of that conviction by the United States Supreme Court a pyrrhic victory. *See United States v. Arthur Andersen, LLP*, 125 S.Ct. 219 (2005). Even if a corporation could face down the threat of criminal prosecution, the specter of parallel civil proceedings and administrative debarment proceedings multiplies the risks and potential costs. In general, the more quickly and thoroughly the corporation conducts an investigation, and the more willing the corporation is to assist in the investigation against its allegedly culpable employees, the more likely the corporation will escape with a deferred prosecution and a fine.

What Can a Corporate Employee/Target Do?

Does any leverage remain for individual officers, directors and corporate employees? Assume that you get a call from a corporate CFO who has received that knock at the door like the one described at the beginning of this article. Often, by the time she calls criminal counsel, she has given a full and un-counseled statement to the attorney conducting the internal investigation, has been fired or put on unpaid leave, and may or may not have a severance package or prospects for employment. In sum, she is on her own, both in terms of her defense costs as well as the corporation's willingness to assist with discovering defense information.

Our hypothetical CFO is, to use a term common in criminal defense circles, "low-hanging fruit." The government has the internal investigation, the corporation's cooperation, and a target without the necessary means to defend herself. The corporation cannot realistically fund her defense and run the risk of being indicted. *See* Thompson Memorandum at 7. ("Another factor to be weighed by the prosecutor [in determining whether to indict the corporation] is whether the corporation appears to be protecting its culpable employees and agents… a corporation's promise of support to culpable employees and agents, either through the advancing of attorneys fees, through retaining employees without sanction for their misconduct, or through providing information to the employees about the government's investigation pursuant to a joint defense agreement.")

Aggravating an already bad situation, federal criminal practice and many analogous state rules do not provide for depositions or formal discovery (except in very limited circumstances, which are beyond the scope of this article). Third-party discovery practice, at least in any formal sense, is quite limited. For example, a third-party witness and documents may be subpoenaed, but need not appear or be produced until the day of trial, absent a court order. Moreover, a federal prosecutor's obligations to provide discovery is limited, requiring for the most part only the disclosure of those items listed in Fed. R. Crim. P. 16. United States Magistrate Judge Mark Pizzo, a former federal public defender and federal prosecutor who has trained innumerable young lawyers on federal discovery issues, has compared federal criminal dis-

covery to evaluating the contents of a large room by looking through a keyhole.

An added pitfall is that the overly zealous criminal defense attorney must avoid even the appearance of witness tampering or obstruction of justice. Because federal criminal procedure lacks discovery, all criminal defense attorneys try to gain critical information through witness interviews. It is received wisdom in the defense bar that many prosecutors scrutinize the manner in which defense counsel conduct these interviews. Even this seemingly basic step in defending a client, then, creates risks. Many key witnesses are themselves often subjects or potential targets who may say anything to garner favor with the government, including lying about what defense counsel said or did during the interview.

Early Dealings with the Government

Returning to our hypothetical CFO, assume that by the time she has found counsel, the now-ubiquitous internal investigation and its attendant interviews are over. After the initial interview, conflict check and engagement letter, her counsel's first step would normally be to determine the client's status with the government. Most criminal defense attorneys simply call the prosecutor and ask, "is Jane Doe a target, witness or subject of your investigation?" (A target is a person against whom the federal grand jury has sufficient evidence to return an indictment. A subject is a person whose activities are of interest to the grand jury and who may become a target. A witness is a person whom the prosecutor has no reason to believe is culpable.) Most prosecutors are quite forthcoming with this information, and indeed, a significant amount of informal "discovery" may occur during the course of this initial discussion.

In that regard, it almost always pays to maintain a professional, tough, but good relationship with the prosecutor. Sometimes a strong, hardheaded non-prosecution presentation and "white paper" to a prosecutor, if done effectively, can actually result in a non-prosecution decision, especially if the alleged conduct is not heartland criminal conduct. The decision to make a presentation is tricky, though. A good prosecutor will always take a presentation of innocence and try to find evidence to rebut it. A good defense lawyer knows that he or she is giving that prosecutor a road map to the defense, but must make a judgment about whether the case for non-prosecution is strong enough to make a no-holds-barred pitch. Each case must be analyzed on its own facts and with a client's full involvement.

At some point in the process, our CFO will likely have to decide whether to speak to the government. This decision is fraught with danger because, even in cases where it is unclear whether the underlying conduct is criminal, the specter of obstruction of justice, perjury or false statement charges looms large. Giving a false statement to the government (or even to a non-government attorney hired by the corporation to conduct the internal investigation) is a crime. This is so even if the statement is not under oath. See 18 U.S.C. §1001. And what makes a statement "false" may surprise you: an aggressive prosecutor may simply decide one version of facts that has emerged from a set of conflicting recollections is the right one. Without the critical documents or other information to prepare a client in advance, advising that your client sit for a government interview is often tantamount to letting him or her walk into a buzz saw.

The hardest decision facing our CFO, of course, is whether to persist in mounting a vigorous defense or whether to accept a guilty plea. There are extremely strong incentives that can cause even those who sincerely believe in their innocence to plead guilty to something. It is no secret that some clients plead guilty to avoid the draconian consequences of persisting through trial. Criminal investigations and trials test the limits of human endurance, both emotionally and financially, because the very process by which closure is obtained in these cases seems more like trial by ordeal than justice. Moreover, a palpable post-Enron backlash, both in terms of the length of potential sentences, as well as a general distrust of corporations among potential jurors, often dictates that we advise clients to plead guilty in ambiguous cases.

If a client ultimately decides to plead guilty, the most opportune time to negotiate a good settlement occurs *before*: i) the government's charging decision has become entrenched; ii) the evidence is fully developed against the client; and iii) the prosecutor has had an opportunity to develop any sort of animus against the client (or her attorney), which can and does happen. At early stages of the case, it is even possible through negotiation to exclude, for sentencing purposes, any information the client provides (assuming that the government does not already have it), such that even culpable conduct will not be considered at sentencing. *See U.S.S.G.* §1B1.8. (The severity of a sentence is based on relevant conduct.) In other words, if the client decides to enter a guilty plea with cooperation in exchange for a reduced sentence, the earlier the decision is made, the better.

Early Dealings with the Corporation

If our CFO were lucky enough to still have her job, her defense counsel's advocacy must extend beyond dealing with prosecutors to dealings directly with the corporation. Although gaining the corporation's assistance is becoming more challenging, the individual does have some bargaining chips. For example, if she has information critical to a defense for the corporation, then her ongoing cooperation and communication with corporate counsel may be viewed as an asset to keep in the corporation's hands. But if her own legal future is put in further jeopardy by speaking to corporate counsel who will waive privilege down the road, she will have to make hard decisions about whether, and to what extent, to continue cooperating with the corporate employer. Most often, cooperation occurs within the context of a joint defense agreement, which most corporations will require as a prerequisite to undertaking to fund its employees' defense.

Even in the landscape created by the Thompson Memorandum, defense counsel for the individual must still try to convince the corporation's criminal lawyer to pursue a global settlement of all charges before the government makes a charging decision. In many cases, the corporation will want to wrap up the entire case and avoid public rehashing of the facts that would occur if the corporation "cut loose" its former employee to the prosecution (or to opposing counsel in any attendant civil cases). Counsel for the individual must maintain close communication with the corporation's attorney in an effort to convince cor-

porate criminal counsel of the reasons why "cutting loose" the individual is neither in the interests of the corporation nor fair to the individual. Most corporate criminal counsel representing large corporations are excellent at what they do, and the prosecutors know it. If corporate criminal counsel has credibility with the prosecutor, he or she can often successfully negotiate a global settlement, particularly if the attorney representing the individual has armed corporate counsel with good reasons for the government not to chase the individual. In all events, the attorney for the individual must work as hard as possible to obtain all possible discovery and assistance before the corporation ultimately decides to cooperate. And this brings us to our next topic: The Joint Defense Agreement.

Operating within a Joint Defense Agreement

No man or woman is an island, and no attorney representing an individual corporate employee can zealously guard a client's interests without seeing the "big picture." As with civil cases, a criminal attorney must plumb the client's knowledge, then plumb the knowledge of the corporate employer and other individuals who played a part in the events under investigation. This typically occurs within the context and constraints of a joint defense agreement, in which discussions between participants to the joint defense are protected by the attorney client privilege.

The joint defense privilege underlies joint defense agreements. That privilege evolved from criminal law practice and is broadly recognized by courts. See In re Grand Jury Subpoena, 902 F.2d 244, 249 (4th Cir. 1990); United States v. McPartline, 595 F.2d 1321, 1336–37 (7th Cir. 1979); Hunydee v. United States, 355 F.2d 183 (9th Cir. 1965); Continental Oil Company v. United States, 330 F.2d 347 (9th Cir. 1964). Theoretically, the joint defense privilege recognizes that, where one or more parties share common interests in a matter, they ought to be able to share information in a privileged manner that furthers those interests. As currently construed, so long as the parties have a common interest and have engaged in a joint effort to defend their clients in actual or potential litigation, the joint defense privilege permits them to share materials without losing the protections of the attorney-client or attorney work product privileges.

The benefits offered by a joint defense agreement can be significant. While client and counsel can gain access to facts, documents, experts and strategies to defend the case, the client is also assured that his or her attorney's duty of undivided loyalty to the client continues. The client's interest in confidentiality is protected because whatever materials are shared among the joint defense group cannot (theoretically) be disclosed to any third parties. Moreover, even if those joint defense materials are subpoenaed or sought through other compulsive means, the typical joint defense agreement requires the party receiving the subpoena to notify the other joint defense members and assert any rights and privileges that would protect the materials from disclosure. With those safeguards in place, sharing materials in a joint defense agreement should not make them significantly more vulnerable to disclosure than they otherwise would have been had they not been disclosed pursuant to that agreement.

A good prosecutor will always take a presentation of innocence and try to find evidence to rebut it.

Participation in a joint defense agreement is not without risk, however, especially where the members' interests begin to diverge. As the criminal case unfolds, it is almost inevitable that one or more of the participants will decide to cooperate with the government, or will otherwise find that their interests are no longer aligned with the other joint defense members. Two key risks can arise. The first is that a conflict of interest may disqualify counsel remaining in the joint defense. This is because, practically, the withdrawing member has shared privileged information that might prove beneficial to the remaining members of the joint defense in cross examining the withdrawing member at trial. The second risk can occur if the attorney-client privilege is considered to have been by the withdrawing member of the group.

Recent case law illuminates these risks and suggests means to avoid them. In *United States v. Henke*, 222 F.3d 633 (9th Cir. 2000), three executives under investigation entered into a joint defense agreement. One executive accepted a plea and testified for the government against the three remaining defendants, all of whom were convicted. On appeal, the convicted executives argued that their own defense counsel should have been disqualified because they were unable to cross-examine the cooperator through the use of statements the cooperating member made at joint defense meetings. The Ninth Circuit reversed the convictions, reasoning that the joint defense privilege established an implied attorney-client relationship between the participating attorneys and all co-defendants, and thus counsel for the convicted executives owed a fiduciary duty to the testifying cooperator that compelled their disqualification.

To avoid a Henke scenario, the joint defense agreement should require three acknowledgements by the participating clients. First, each client should acknowledge that no attorney-client relationship has been formed between the client and other attorneys within the joint defense group. Second, each counsel and client should make a knowing waiver of all potential conflicts of interest that may arise as the result of the joint defense. Third, each client should expressly acknowledge that none of the participating attorneys should be prevented from examining or cross-examining any party who testifies at any proceeding on the basis of information learned during the joint defense.

The flip-side of the disqualification issue raised in Henke occurs where a withdrawing member of a joint defense agreement cooperates with the government and then waives the attorney-client privilege and tells the government about communications that the withdrawing member shared with other joint defense counsel. See United States v. Almeida, 341 F.3d 1318, 1326 (11th Cir. 2003). The court in Almeida held that a cooperrator who joins forces with the government waives the privilege as to communications he or she made directly to joint defense counsel. The Almeida court recognized that its holding somewhat chipped away at the principles underlying joint defense agreements, but it considered such

a threat minimal, reasoning that: "Making each defendant somewhat more guarded about the disclosures he makes to the joint defense effort does not significantly intrude on the function of joint defense agreements."

Read together, *Almeida* and *Henke* suggest a practice that, for the most part, has already been adopted by most criminal defense attorneys. Joint defense communications, in fact, do not involve conversations with defendants at all but occur among the attorneys whose clients are participating in the joint defense. Permitting a client to speak directly to other joint defense counsel creates an inherent conflict of interest, as well as a potential for waiver of the privilege.

Of course, this approach poses a problem for a represented corporate employee whom the corporation wishes to interview as part of its internal investigation. In that context, the attorneys for both the employee and the corporation must have a clear understanding whether the corporation wishes to preserve the right to waive the attorney-client privilege down the road. See United States v. LeCroy, 348 F. Supp. 2d 375 (E.D.Pa. 2004) (joint defense privilege deemed waived by corporate employee who was interviewed by corporate counsel who expressly reserved the right to share internal investigation with the government). The government's current emphasis on early and full cooperation by a corporation under investigation means that counsel for both the individual and the corporation must have a clear agreement as to whether their interests are common.

Advancement of Legal Fees and Indemnification

Both our CFO and her counsel will need to know up front whether and how her defense will be funded. Corporate charters, bylaws, and many state corporation codes require corporations to make payments to current and former officers and directors to enable them to pay for attorneys and other costs of defending themselves in criminal and civil actions brought against them by reason of their management positions and board service. Sound policy reasons justify this; encouraging corporate officials to resist unjustified lawsuits encourages capable individuals to serve as corporate officers. *Hibbert v. Hollywood Park, Inc.*, 457 A.2d 339, 343–44 (Del. 1983). Further, indemnification encourages capable people to serve as directors and officers secure in the knowledge that the corporation will absorb the cost of defending their integrity. *VonFeldt v. Stifel Fin. Corp.*, 714 A.2d 79, 81 n.4 (Del. 1998).

Delaware's indemnification statutes merely permit a corporation to indemnify certain protected persons. A director or officer is not *entitled* to indemnification unless the corporation's certificate of incorporation, bylaws or some other corporate document mandates the indemnification. Moreover, under the Delaware statute, indemnification is only permitted if the person acted in good faith in a manner he reasonably believed to be in, or not opposed to the best interests of the corporation. Del. Stat. section 145 (a) & (b). With respect to criminal proceedings, the person must also have had no reasonable cause to believe the conduct was unlawful. Interestingly, conviction or plea does not, alone, create a presumption that the individual's conduct did not satisfy this standard. *Id.* Indeed, a corporation may even be required to indemnify an officer who pleads guilty. *Maiss v. Bally Gaming Int'l*, 1996 WL 732530 (E.D. La. Dec. 12, 1996).

Unfortunately, attorneys representing individuals must often be prepared to sue the corporation to obtain advancement of fees or indemnification. Even where the board of directors of a corporation has not agreed to indemnify an individual, a court can make its own de novo determination whether the standards for indemnification were met. Where a state statute permits indemnification or advancement, and where the corporate bylaws, articles of incorporation, or some other corporate document have allowed it, a protected individual may sue for indemnification or advancement in state court on a breach of contract theory. Indeed, under certain circumstances, a prevailing party seeking indemnification may be awarded "fees for fees," or the fees associated with enforcing the contractual right to indemnification or advancement. Although a detailed analysis of this complex and evolving area of the law is beyond the scope of this article, for an excellent discussion of current developments, see K. Valihura and R. Valihura, Recent Developments in Indemnification and Advancement of Litigation Expenses, 7 Del. L. Rev. 65 (2004) (describing numerous such lawsuits).

Conclusion

Defending corporate employees in criminal cases has become far more delicate and difficult than ever before. As things currently stand, the factors conspiring against individual white collar defendants, from the sentencing guidelines to the Thompson memorandum to Sarbanes Oxley, can overpower the individual who lacks an extremely strong will and an extremely deep pocket.

There may be help on the way though. On August 9, 2005, the ABA House of Delegates approved a resolution calling on federal regulators to stop pressuring organizations into waiving their attorney-client privilege and work product protection to avoid appearing uncooperative in civil and criminal investigations. The resolution, drafted by the ABA's task force on Attorney-Client Privilege, held public hearings on the issue and submitted its recommendations to the House of Delegates. The text of the resolution "strongly supports" the preservation of the attorney-client privilege because it is essential to the proper and efficient functioning of the American adversary system of justice. That resolution opposes government policies and practices that have the effect of eroding the attorney-client privilege and work product doctrine. Finally, it opposed "the routine practice by government officials of seeking to obtain a waiver of the attorney-client privilege or work product doctrine through the granting or denial of any benefit or advantage."

Further, there are concrete steps we attorneys can (and should) take to ensure the preservation of the attorney-client privilege. N. Richard Janis, who wrote an excellent article on this issue entitled Deputizing Company Counsel as Agents of the Federal Government: How Our Adversary System of Justice is Being Destroyed, has noted the increasing attention this issue is receiving, not only among lawyers, but in the press as well. He has prepared a list of suggestions as to how we lawyers might restore some balance to the adversary system of justice, including lobbying states to: 1)

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require indemnification and advancement of legal fees for employees; and 2) prohibiting companies from requiring employees to submit to interviews if there is any chance those interviews will be provided to the government. Janis also suggests we attorneys lobby the U.S. Sentencing Commission to eliminate corporate privilege waivers as factors mitigating corporate sentences, that state Bars change the ethics rules to require very specific instructions regarding employee waivers of their rights, and that we assist in mounting legal challenges to companies sharing coerced interview results with the government. Janis makes several more excellent suggestions in this regard, and we urge our civil practitioner colleagues to speak up on this critical issue. FD