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# Business Crimes Bulletin®

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## Ten Tips for Handling Sensitive Investigations

### *Practical Advice You Need in the Sarbanes-Oxley Era*

**By Robert W. Tarun**

The Enron, Tyco and WorldCom scandals have greatly heightened the fiduciary duties of directors and officers and the scrutiny paid to them. The spotlight on corporations and their managers is likely to shine brightly for years to come. This article offers ten practical tips for handling sensitive investigations in an era where shareholders, prosecutors, regulators and courts are likely to scrutinize the response of organizations to inevitable episodes of suspected corporate misconduct.

***1. Consider whether an outside law firm with little or no relationship to the company will better serve the objectives of an independent investigation.***

In matters potentially implicating senior corporate executives, the Board of Directors or Audit

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## Court-Imposed Waiver of the Joint-Defense Privilege

**By Jacqueline C. Wolff and Alan Vinegrad**

Most defense attorneys enter into joint-defense agreements with the understanding that even if one of the signatories decides to withdraw from the agreement and cooperate with the government, the confidentiality provisions survive. Such agreements routinely include language like this:

"In the event that any client … engages in negotiations or enters into any agreement with any third party that is in any respect … inconsistent with the continued sharing of information under this Agreement, such client shall be deemed to have withdrawn from this Agreement and shall refrain from disclosing to the third party any joint-defense materials.

No attorney who has entered into this Agreement shall be disqualified from cross-examining any client to this Agreement … because of … [this] Agreement; however, nothing herein shall permit any attorney to cross-examine another attorney's client utilizing any joint-defense material contributed by that client."

Two recent decisions — by the Eleventh Circuit and the Northern District of California — have called provisions like these into question: *United States v. Almeida*, 341 F.3d 1318 (11th Cir. 2003); and *United States v. Stepney*, 246 F. Supp.2d 1069 (N.D. Cal. 2003). Any defense attorney who is considering entering into such an agreement should think twice — especially if some party may choose, down the road, to cooperate with the government.

For years it has been well established that "a joint defense agreement cannot be waived without the consent of *all* parties to the privilege" since allowing unilateral waiver "would 'whittle away' the privilege." *United States v. Weissman*, 1996 WL 737042 at *26 (S.D.N.Y. Dec. 26, 1996) (emphasis added); *In the Matter of Grand Jury Subpoena Duces Tecum Dated November 16, 1994*, 406 F. Supp 381, 394 (S.D.N.Y. 1975). Further, "a waiver by one party to a joint defense agreement does not waive any other party's privilege over the same communications." *Securities Investor Protection Corp. v. Stratton Oakmont, Inc.*, 213 B.R. 433, 436 (S.D.N.Y.

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## *Joint-Defense Privilege*

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1997). The only exception is when the parties subsequently become adversaries in litigation. *Id*. Even then, the waiver is only as to each other.

### *Stratton Oakmont*

In *Stratton Oakmont*, the government argued that it was entitled to joint-defense material because the parties to the joint defense agreement became adversaries in a subsequent litigation. The court rejected the government's argument, stating the fact that the signatories had become adversaries did not mean that the "rest of the world suddenly becomes entitled to privileged information." *Id*. at 438.

Under the standard no-waiver provision, a client runs the risk of having his or her attorney disqualified because of an inability to use joint-defense information during cross-examination. Nevertheless, courts have generally not second-guessed the client's assumption of this risk. Potential defendants are so disadvantaged vis-à-vis the government in evidence-gathering that the risk of potentially losing one's lawyer is small compared with the risk of not having the facts with which to prepare an effective defense. Indeed, at least one court has even deemed the acceptance of this risk tantamount to a waiver of any conflict. *United States v. Anderson*, 790 F. Supp. 231, 232 (W.D. Wash. 1992).

### The *Stepney* and *Almeida* Cases

The *Stepney* and *Almeida* decisions, however, chart a very different course. Both cases held that when a party to a joint-defense agreement testifies on behalf of the government, that party may be cross-examined with statements he or she made pursuant to the joint-defense agreement.

In *Stepney*, the government charged almost 30 defendants in a series of indictments with 70 counts, including participation in a street gang. Defense counsel, some of whom had never met prior to the indictments, entered into joint-defense agreements to try to prepare a coherent defense to this massive case. In order to ensure that each of the defendants' Sixth Amendment rights were protected, the court ordered that any joint-defense agreements would have to be memorialized in writing and submitted for *in camera* review.

The agreement provided that any signatory could withdraw at any time, each signatory accepting the risk that his or her attorney might then be conflicted out of representing him or her at trial. The court recognized that in this type of multi-defendant case, deals with the government could occur at any time for any number of defendants and enforcing disqualification could create a revolving door of attorneys leading to adjournments and prejudice to all parties. Were one party to testify for the government, *all* the remaining defense attorneys could be disqualified.

The court also rejected the standard provision in which the signatories simply agree not to use joint-defense information to cross-examine a party who withdraws from the agreement. "This method of waiving conflict … stands in tension with the general principle that where an attorney has actually obtained confidential information relevant to her representation of a client, the law presumes she cannot avoid relying on the information — however indirectly or unintentionally — in forming legal advice and trial strategy." 246 F.Supp.2d at 1085. Instead, the court, citing the ALI-ABA model joint-defense agreement, ruled that any signatory who withdraws from a joint-defense agreement and testifies may be cross-examined with any material he contributed to the joint defense and that joint-defense agreements "must contain" a provision specifically waiving confidentiality should a signatory choose to testify.

*Almeida* involved two parties to a joint-defense agreement, one of whom decided to cooperate with the government. At trial, the attorney for the non-cooperating defendant sought to cross-examine the cooperator with statements he made during

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# State Proceedings and Confidentiality Agreements with the Federal Government

**By Avi S. Garbow**

When management or the Board of Directors suspects possible misconduct within the company, they cannot respond with sound business judgment unless they have good information about what happened. In serious cases, they probably need outside counsel to investigate, report, and recommend remedies. The government has long encouraged companies to disclose the results of these internal investigations by offering the hope of leniency in charging or sentencing. On Sept. 22, 2003, the Attorney General added a "stick" to this "carrot" approach when he announced the Justice Department's new policy of charging the most serious criminal offenses that are readily provable, with a limited exception in cases where a defendant provided substantial assistance.

While companies frequently elect to disclose to the federal government under these, and related, policies, whether or not third parties can get the information disclosed to the government is a rapidly evolving open question. The key issue in this debate is a company's ability to predict, and in actuality to control, the ultimate dispersion of its confidential information once disclosed to the federal government. In *In re: WorldCom, Inc. Securities Litigation,* 02 Civ. 3288 (DLC) (S.D.N.Y.) (WorldCom), one district court recently adopted a United States Attorney's Office (USAO) proposal creating tiers of disclosure of the company's work product. In *U.S. v. Bergonzi, et al.,* No. 03-10024 (9th Cir.) (McKesson), the United States and the cooperating corporation appealed the lower court's decision to order disclosure of McKesson HBOC's work product to former employees who were under indictment.

While federal courts are struggling with the tension between cooperation and confidentiality, the state of Oklahoma indicted WorldCom despite the company's cooperation with the SEC and U.S. Attorney in New York. The trend toward parallel state proceedings means that federal courts may be powerless — absent new preemptive legislation — to protect confidentiality in return for cooperation with federal prosecutors and agencies.

### *WorldCom* and *McKesson*: Cracks in the Armor

On June 12, 2002, Cynthia Cooper, a WorldCom vice president for internal audits, informed the chairman of its Audit Committee about the series of questionable transfers during 2001 and 2002 that would grow into a $3.8 billion accounting scandal. Within 2 weeks, WorldCom announced that it had retained Wilmer Cutler & Pickering to conduct an independent internal investigation.

The company president published an open letter to President Bush affirming WorldCom's commitment to working with the federal investigators, and its Chairman of the Board similarly pledged his cooperation before the House of Representatives' Financial Services Committee Hearing on July 8, 2002. The Wilmer team agreed to allow government investigators to be present during some of their employee interviews, and also agreed to certain governmental requests to limit the scope of their inquiries (or in some cases, not to interview certain persons). The Special Investigative Committee of WorldCom's Board agreed to provide certain interview memoranda and the underlying collection of documents to both the U.S. Attorney's Office in the Southern District of New York and to the SEC. These agreements, the terms of which were memorialized in a series of letters, specified:

"By agreeing to produce the Subject Documents, the Committee does not intend to waive any protection of the work-product doctrine or the attorney-client privilege as to any third party, and intends only to effect a limited waiver as to the Office with respect to the Subject Documents only … The Office agrees to maintain the confidentiality of the Subject Documents in the manner provided by Rule 6(e) of the Federal Rules of Criminal Procedure with respect to the documents and testimony provided to a grand jury, and the Office will not disclose the Subject Documents at any time, except (1) … the Office agrees to make the Subject Documents available to SEC representatives only in the event that the SEC enters into a confidentiality agreement with counsel to the Committee regarding the Subject Documents; and (2) to the extent the Office, in its sole discretion, determines that disclosure is required by law or court order; such as, for example, pursuant to Rule 16 … or [18 U.S.C. §] 3500." (*Oct. 9, 2002 letter from Charles Davidow (Wilmer) to David Anders* (USAO/SDNY)) (emphasis added).)

"The Staff will maintain the confidentiality of the Confidential Materials pursuant to this agreement and will not disclose them to any third party, except to the extent that the Staff determines that disclosure is otherwise required by law or would be in furtherance of the Commission's discharge of its duties and responsibilities." (*Oct. 10, 2002 letter from Charles Davidow to SEC*) ((emphasis added).)

### Supboena *Duces Tecum*

Wilmer Cutler & Pickering issued its internal investigative report (hereinafter "WorldCom Report") on March 31, 2003, and WorldCom's Board publicly released it on June 9, 2003. Less than 2 weeks later, Arthur Andersen, a party in the *WorldCom* civil fraud actions — in the Southern District of New York, served a subpoena

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## State Proceedings

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*duces tecum* upon Wilmer essentially seeking all documents, including drafts and attorney notes, related to the WorldCom Report. Wilmer refused to comply with the subpoena. Arthur Andersen moved to compel production, arguing that WorldCom waived any attorney-client privilege or work product protection by publicly announcing its intention to release the Report, by allowing government investigators to participate in its investigation, and by disclosing the material to the government. Bernard Ebbers, a defendant in a pending related criminal action, joined the motion, adding that disclosure was required by Rule 16 and *Brady v. Maryland*, 373 U.S. 83 (1963). The U.S. Attorney and the S.E.C. joined Wilmer in opposing the motion primarily on the basis of the existence of confidentiality agreements governing the disclosure.

Shortly thereafter, the U.S. Attorney's Office obtained the consent of Arthur Andersen, Ebbers, and WorldCom to a proposed resolution of the pending motion to compel. Specifically, the parties agreed to: "1) a rolling, tri-part production of the Wilmer documents, pursuant to a confidentiality agreement and protective order, and 2) a staggered schedule for depositions, which would allow certain depositions to proceed forthwith but also ensures that (a) depositions of the defendants are stayed (at least) pending production of most of the Wilmer documents, and (b) Government witnesses are not deposed until they have testified at any criminal trial." (Sept. 4, 2003 letter from William Johnson and Meredith Kotler (USAO/SDNY) to the Hon. Denise L. Cote).

Judge Cote gave her imprimatur to this ad-hoc compromise, which served the government's parochial interests in its criminal case, but failed to safeguard WorldCom's potential long-term interest in confidentiality or advance the law toward a solution of the recurring conflict between protecting confidentiality and cooperating with law enforcement.

### McKesson's Confidentiality Agreements

*McKesson* also involved the creation and disclosure of an internal investigative report. Soon after McKesson HBOC publicly disclosed accounting irregularities uncovered by its auditors, the company's Audit Committee retained Skadden, Arps, Slate, Meagher & Flom to conduct an independent internal investigation. McKesson entered into confidentiality agreements with the SEC and the United States Attorney for the Northern District of California containing terms nearly identical to those in *WorldCom*, and pledged to turn over a copy of its internal investigative report (the "McKesson Report") and back-up materials.

Jay Gilbertson and Albert Bergonzi, former executives of HBOC, were indicted and moved under Rule 16 and *Brady* to compel production of the McKesson Report. McKesson intervened and opposed production on the grounds that the Report and Interview Memoranda were protected by the attorney-client privilege and the work product doctrine. Judge Jenkins granted the defendants' motion to compel. *See US v. Bergonzi*, 216 F.R.D. 487 (N.D. Cal. 2003). McKesson appealed, and later appealed a similar order obtained at the request of subsequently indicted defendants. The appeals were consolidated, and briefing is to be completed on Jan. 30, 2004 under the terms of a pending status report.

### The Oklahoma Indictment

While the parties in WorldCom and McKesson were briefing the discoverability issue regarding their respective internal reports, Oklahoma Attorney General Drew Edmondson approved State criminal charges against WorldCom, Inc. and several of its former executives. Edmondson's office provided no advance notice of the charges to the federal investigative team already assembled in the WorldCom matter, and he explained his decision to file criminal charges against WorldCom by calling the record $750 million WorldCom civil settlement "totally inadequate." The charges drew the immediate ire of U.S. Attorney James Comey in New York, who was "disappointed that we were not told that charges were imminent as we have enjoyed a cooperative relationship with the Attorneys General of other states." After fully cooperating with the federal agencies and disclosing its Report pursuant to confidentiality agreements, WorldCom now faces its first criminal charges arising from the scandal.

Oklahoma was not alone. New Mexico hired Milberg Weiss LLP to handle a trio of securities fraud lawsuits against WorldCom and its former executives seeking over $80 million, and other states including West Virginia, Oregon, Alabama, and Arkansas are waiting in the wings.

This parallel enforcement activity comes on the heels of a new SEC and state joint enforcement initiative announced by SEC Chairman William Donaldson on Sept. 14, 2003. This cooperative enforcement initiative is presumably responsible for the nearly simultaneous announcements on Oct. 28, 2003 by the SEC and the Commonwealth of Massachusetts of civil fraud charges against Putnam Investments. Significantly, Chairman Donaldson noted that in the past 2 years, the SEC's Division of Enforcement has granted more than 250 requests from state and local government entities for access to the SEC's investigative files.

The proliferation of state causes of action will shift the debate over confidentiality to the state courts, where the common law may hold the privileges waived or destroyed notwithstanding any confidentiality agreement approved by a federal district court. Moreover, the confidentiality agreements entered into in *WorldCom* and *McKesson*, for example, arguably permit disclosure to states that elect to prosecute their own securities actions, particularly if such state actions are couched in terms of a joint initiative with the federal government. Whereas the federal government may seek to retain the ability to disclose in certain circumstances, companies should, at a minimum, preserve their interests by requiring notice of any third party requests for confidential information

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## Ten Tips

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Committee should consider whether counsel conducting investigations should be from a law firm that the company regularly uses as outside counsel or that derives a material amount of revenues from the company. For example, in the Enron case, the firm had collected more than $100 million in legal fees from Enron, and its partners had provided legal advice in the transactions it later investigated. Issues of independence and self-interest clouded the credibility of the law firm's internal investigation.

If there is a serious question whether the outside law firm or the investigation counsel in that law firm will have the necessary objectivity and independence, the better course is to retain an experienced law firm with minimal or no historic relationship to the company or management.

***2. Carefully define the scope of the investigation at the outset.***

The client (the corporation, the Board of Directors or Audit Committee) and investigating counsel must take great care to define the scope of the investigation at the outset of the engagement. If the scope is drawn too narrowly, stakeholders and government authorities will dismiss the purpose, objectivity and use of the report, or later criticize any failure to review possible misconduct that was outside the narrowly drawn scope. If drawn too broadly, an investigation can be aimless and continue indefinitely with no meaningful benefit to the client. The client mandate should be reduced to writing and allow for expanding or redefining the investigation if unforeseen issues arise.

***3. Promptly take steps to secure all relevant documents.***

Many corporate internal investigations arise at a point when a government inquiry or investigation is known, imminent or probable. The Sarbanes-Oxley Act of 2002 (the Act) broadened the reach of obstruction of justice statutes. *See* 18 U.S.C. § 1519 (2002). To ensure that the corporation and its employees are not investigated or prosecuted for obstruction of justice, counsel in an investigation should take prompt steps to secure and preserve relevant original documents. In transnational investigations, counsel should carefully consider whether the transfer of documents from their original location will provide jurisdiction over documents that would not otherwise exist. Documents kept out of the jurisdiction must still be preserved since the inferences that would be drawn from spoliation are invariably disastrous.

***4. Make clear to employees that investigating counsel do NOT represent them.***

Many employees mistakenly believe that interviewing counsel represent their interests during investigation interviews. Counsel must give *Upjohn* warnings to officers and employees, making clear the nature and purpose of the investigation, whom counsel represents (*ie,* the corporation and not the officer or employee), the privileged nature of the interview, and who retains the privilege (*ie,* the corporation). Otherwise, there is a clear risk of litigation over use, waiver and admissibility of interview statements. Memoranda of interviews should reflect the *Upjohn* preamble that investigating counsel have provided to interviewees.

***5. Ensure that investigating counsel avoid or at least minimize public statements about the internal investigation.***

Investigating counsel conduct internal investigations in order to provide confidential legal advice to clients. If counsel or the client makes public statements about the investigation, courts may conclude that it was motivated by business necessities and public relations and is not privileged. *See In re Kidder Peabody Securities Litigation*, 168 F.R.D. 459, 465-455 (S.D.N.Y. 1996).

***6. Keep in mind that a written report will in many cases be appropriate.***

Whether a company is best served by a written or oral report will turn on the facts of each situation. *See* Webb, Tarun and Molo, Corporate Internal Investigations, § 11.03 (Law Journal Seminars Press 2003).

In the Sarbanes-Oxley era, stakeholders and government agencies may view an oral report with skepticism in the wake of serious allegations of corporate misconduct. A written report better assures that the company, the board of directors and relevant committees will undertake a full review of the issues, understand the prescribed legal advice, and implement recommended remedial action.

***7. Assume any written report may ultimately be released to the public.***

Counsel must take all steps to protect the privileged nature of a report, the underlying interviews, other factual investigation and legal research. Still, counsel should assume that in the current prosecutorial, regulatory and shareholder climate, any written report will be released at some point to government agencies or parties other than the client. The "Federal Prosecution of Business Organizations" policy (Department of Justice: January 20, 2003) states that one of the nine factors in reaching a decision as to the proper treatment of a corporate target is the corporation's timely and voluntary disclosure of wrongdoing and its willingness to cooperate in the investigation of its officers and employees, including, if necessary, the waiver of corporate attorney-client and work product protection. The Commentary to this important policy provides that certain factors may be weighted more or less than others depending upon law enforcement priorities. Prosecutors and regulators have been increasingly aggressive in seeking written reports of corporate investigations, and counsel should anticipate this possibility while conducting an investigation and preparing a written report.

***8. Understand that a report should be written for multiple audiences.***

Given the likelihood that a written report may ultimately reach the public, counsel should draft it with great care and with all potential audiences in mind. Stakeholders of a

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## *Joint-Defense Privilege*

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joint-defense meetings. The government objected on the grounds of the joint-defense privilege. The witness, while not revealing joint-defense material, conceded to the court that the information would be useful both in cross-examining him and in locating defense witnesses. Nonetheless, the court sustained the objection. After the defendant was convicted, the cooperator revealed that the defendant was, in fact, not guilty and that he had told the defendant's attorney as much during a joint-defense meeting.

The Eleventh Circuit, citing *Stepney*, reversed. The court said the "justification for protecting the confidentiality" of joint-defense communications "is weak" and that "little can be gained by extending the [attorney-client] privilege" to joint defense communications." 341 F.3d at 1324. The court only grudgingly acknowledged that "in light of the vast resources of the government" it is "perhaps appropriate" that co-defendants be allowed to exchange information confidentially.

The court then went on to rule that, when a party to a joint-defense agreement later testifies for the government, he may be cross-examined with his joint-defense communications. Citing a 1957 A.L.R. article and a 115-year-old Michigan case, the court concluded that it is an "ancient rule" that, when a defendant turns state's evidence, he waives any privilege he may have had with his *own* attorney. Although the court stopped short of ruling that accomplices *always* waive the privilege when they testify for the government, it did hold that, "when each party to a joint defense agreement is represented by his own attorney, and when communications by one co-defendant are made to the attorneys of the other co-defendants, such communications do not get the benefit of the attorney-client privilege in the event that the codefendant decides to testify on behalf of the government in exchange for a reduced sentence." In a footnote, the court stated that "[i]n the future" defense attorneys "should insist" that joint-defense agreements contain a "clear statement of the waiver rule enunciated in this case[.]"

The implications of these decisions are potentially far-reaching. Whereas in the past the courts left it up to the parties to decide what risks they were willing to accept in signing joint-defense agreements, the *Stepney* and *Almeida* courts have stepped in and pronounced which waivers they believe are acceptable, even going so far as to require defense counsel to include such provisions in their joint-defense agreements.

Although these rulings may avoid the sort of injustice that occurred in

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## *Ten Tips*

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corporation include shareholders, employees, lenders, customers, vendors, the communities where the company operates and conducts business. Stakeholders are likely to be contacted by the media, so journalists are also an important potential audience. Potential government audiences include law enforcement authorities such as the Department of Justice, U.S. Attorney offices, FBI, and state attorneys general; regulatory agencies such as the SEC; and legislative bodies including Senate and House committees. Other important potential audiences are self-regulatory organizations (SROs) and federal, state and municipal licensing authorities.

***9. Investigating counsel must be ever-mindful of process when representing a Board of Directors, Audit Committee or Special Committee.***

Under the business judgment rule, reviewing courts focus largely on the *manner* in which a director performs his or her duties — not the correctness or wisdom of the decision. Likewise, prosecutors and regulators such as the SEC will examine the process under which an investigation was conducted. Sarbanes-Oxley expressly encourages corporate officers to seek and rely on expert advice from outside counsel and others. If counsel and the client do not thoroughly examine the facts, review the issues and consider and implement remedial actions, the investigation may not earn the company any credit and, in fact, can harm the interests of the corporation and its shareholders.

Counsel must therefore be mindful of process in representing the client. You should explain the nature of the investigation, the likely course of the investigation, the potential legal risks, disciplinary options and remedial actions available to the company. To protect the corporation, there should be a clear record of the process and care with which the directors have reviewed and addressed the matters at issue.

***10. Counsel and client must follow through on recommendations to remedy problems at hand and prevent recurrence of the problem(s) that led to the investigation.***

It is rare that an investigation of corporate misconduct or misfeasance will not lead to formal or informal recommendations to the Board of Directors, Audit Committee or a special committee. Once a crisis subsides, the client often becomes occupied with other business and fails to ensure that recommendations have been implemented to minimize the reoccurrence of similar problems.

If new corporate misconduct later comes to light, prosecutors and regulators will likely review the company's response to prior incidents when they make charging or enforcement decisions. New directors and officers will in most instances be held responsible for familiarizing themselves with past governance problems and ensuring that management has in fact implemented recommendations.

# BUSINESS CRIMES HOTLINE

## FLORIDA

### Rhino Ecosystems Executives Plead Guilty

Charles Joseph Cini, former president of Rhino Ecosystems Inc. (Rhino), and Mark Wiertzema, former chief financial officer, pleaded guilty in the United States District Court for the Southern District of Florida to conspiracy to commit wire and securities fraud. Rhino is a publicly traded corporation that purportedly developed and marketed a grease-trapping filtration plumbing product for restaurants and food-processing businesses.

According to the indictment, Cini, Wiertzema and their co-defendants allegedly agreed to pay approximately $6 million in an undisclosed kickback to an undercover FBI agent and others to induce a fictitious foreign mutual fund to buy approximately 650,000 shares of overpriced Rhino stock for a total of $8.6 million. Cini and Wiertzema also allegedly agreed to assist in artificially increasing the market price of Rhino stock upon the sale of the 650,000 shares of Rhino stock and were to receive a portion of the undisclosed kickback payment for their role in the stock transaction.

Cini and Wiertzema each face a maximum statutory sentence of 5 years' imprisonment on the conspiracy count and a fine of up to $250,000.

## ILLINOIS

### Former Chairman and CFO of Anicom Indicted in Corporate Fraud Scheme

Scott Anixter, former chairman of the board of the now-defunct Anicom, Inc., and former Chief Financial Officer Donald Welchko were indicted in Chicago for allegedly engaging in a corporate fraud scheme by inflating sales and revenues by tens of millions of dollars beginning approximately 3 years before the company went bankrupt. According to the indictment, Anixter and Welchko, along with various co-schemers, allegedly created fictitious sales of at least $24 million, understated expenses, and overstated net income and earnings by millions of dollars, knowing that the materially false financial information was being provided to investors, auditors, lenders and security regulators.

Anicom was a national distributor of wire and cable products, such as fiber optic cable, based in Rosemount, Illinois. Anicom's shares were publicly traded on NASDAQ until trading was halted on July 18, 2002, when Anicom announced that it was conducting an investigation into possible accounting irregularities and that investors should not rely on its 1998 and 1999 financial statements.

Both Anixter and Welchko were each charged with three counts of securities fraud, five counts of bank fraud, five counts of making false statements to financial institutions, and seven counts of making false statements to the SEC. Welchko alone was charged with an additional count of making false statements to the SEC, four counts of falsifying Anicom's financial books and records, and a single count of obstruction of justice in connection with the SEC's investigation.

If convicted of securities fraud, Anixter and Welchko each face a maximum penalty of 10 years in prison and a $1 million fine on each count. The remaining charges against Welchko and Anixter carry the following maximum penalties on each count: bank fraud and making false statements to financial institutions — 30 years' imprisonment and a $1 million fine; making false statements to the SEC — 5 years' imprisonment and a $250,000 fine; and falsifying books and records — 10 years' imprisonment and a $1 million fine. The obstruction charge against Welchko carries a maximum penalty of 5 years' imprisonment and a $250,000 fine. The fine may be increased to twice the gain derived from the crime or twice the loss suffered by the victims of the crime, if either of those amounts is greater than the statutory maximum fine.

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## *Joint-Defense Privilege*

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*Almeida* by enabling defense counsel to show that a government cooperator is simply fabricating a story to help himself, the justification for the judicial altering of the balance of benefits and risks inherent in joint-defense agreements is open to question. Why not enforce an agreement that permits withdrawal without any risk of disqualification by limiting the use of joint-defense statements in cross-examination?

### Other Concerns

Other concerns were not even addressed in these decisions. How will a prosecutor fully debrief a cooperator about his or her joint-defense statements in order to be prepared for any potential impeachment on cross-examination? Won't he or she need to know the other side of the conversation to understand the cooperator's statements fully? Will a prosecutor use *Stepney* and *Almeida* to justify obtaining *all* the joint-defense communications?

Moreover, the rulings may jeopardize the privilege of a *non-cooperating* defendant who testifies on his or her own behalf. Indeed, the court in *Stepney* ruled that its mandatory waiver provision covers "*any* defendant who testifies at *any* proceeding, whether under a grant of immunity or otherwise." 246 F.Supp.2d at 1086 n.21 (emphasis added).

If a non-cooperating defendant gave testimony contrary to his joint-defense statements, could a cooperator reveal this to the prosecutor, and could the prosecutor then use those statements to cross-examine the defendant? If a non-cooperating defendant testified and sought to shift blame onto his or her co-defendant in a manner contrary to his joint-defense statements, would these courts uphold the co-defendant's use of those statements in cross-examination? After *Stepney* and *Almeida*, the answers to these questions are far from clear, no matter what the joint-defense agreement may provide.

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# IN THE COURTS

## HEALTH CARE FRAUD STATUTE COVERS MORE THAN HEALTH CARE

*In a Matter of First Impression, the Second Circuit Holds that the Federal Health Care Fraud Statute Broadly Covers a Wide Range of Conduct and Is Not Restricted to Health Care Providers.*

In *United States v. Lucien*, Nos. 02-1228, 02-1266, 02-1395, 2003 WL 22333062 (2d Cir. Oct. 14, 2003), the defendants appealed their conviction under the health care fraud statute, 18 U.S.C. § 1347. The defendants had been convicted under 18 U.S.C. § 1347 for their participation as passengers in staged automobile accidents designed to profit from New York's no-fault automobile insurance program. On appeal, the defendants contended that the federal health care fraud statute only applies to health care professions and that they did not defraud a "health care benefit program," as prohibited in the statute, by defrauding the New York State no-fault automobile insurance program.

The health care fraud statute, 18 U.S.C. § 1347, states: "Whoever knowingly and willfully executes, or attempts to execute, a scheme or artifice — (1) to defraud any heath care benefit program; or (2) to obtain, by means of false or fraudulent pretenses, representations, or promises, any of the money or property owned by, or under the custody or control of, any health care benefit program, in connection with the delivery of or payment for health care benefits, items, or services, shall be fined under this title or imprisoned not more than 10 years, or both." The relevant definition of a "health care benefit program" is set out in 18 U.S.C. § 24(b), which provides: "As used in this title, the term 'health care benefit program' means any public or private plan or contract, affecting commerce, under which any medical benefit, item, or service is provided to any individual, and includes any individual or entity who is providing a medical benefit, item, or service for which payment may be made under the plan or contract."

In a matter of first impression, the Second Circuit found that the defendants' argument that the statute only applies to health care professional is at odds with the plain language of the statute that states "[w]hoever knowingly and willfully executes, or attempts to execute a scheme or artifice … to defraud any health care benefit program … " The court found the common meaning of the term "whoever" to cover any person. While acknowledging that resort to legislative history was not necessary due to the plain language of the statute, the court also found that the legislative history of the statute supported the court's construction because the defendants' specific conduct was envisioned by Congress when it enacted § 1347.

Moreover, the court rejected the argument that the health care fraud statute did not apply to their conduct because the New York State no-fault automobile insurance program does not operate nationwide and thus could not constitute a health care benefit program within the meaning of the statute. The court found no such limitation in the statute, which provides simply that "any public or private plan or contract … under which any medical benefit, item, or service is provided to any individual" qualifies as a "health care benefit program" under § 24(b). Because the defendants received a "medical benefit" as a result of the vehicle owners' no-fault "insurance contracts," the court held that a health care benefit program is plainly implicated under § 24(b). Thus, the court affirmed the defendants' convictions under 18 U.S.C. § 1347 based on their participation as passengers in staged accidents designed to profit from New York's no-fault insurance regime.

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## *State Proceedings*

*continued from page 4*

prior to disclosure in order to allow them to intervene when appropriate.

### CONCLUSION

Obsession with confidentiality should not be allowed to diminish the benefits of a full and comprehensive independent investigation. But corporate counsel must weigh the risks associated with possible related criminal and state enforcement actions when deciding upon an initial voluntary disclosure strategy. *Brady* concerns, Rule 16 requirements, and cooperative state-federal enforcement initiatives may compromise counsel's ability to control third-party access to confidential information.

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