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Second Circuit Rules Against DOJ in KPMG
Prosecution While DOJ Revises Policy on Corporate Prosecutions

Delivering a perhaps decisive victory to defendants in this high-profile matter, the U.S. Court of Appeals for the Second Circuit on August 28, 2008, upheld the dismissal of all charges against thirteen former partners and employees of KPMG, holding that the government had violated defendants' Sixth Amendment rights by pressuring KPMG to cut off payment of their legal fees. [*U.S. v. Stein*, 07-3042 \(2d Cir. Aug. 28, 2008\)](#). The Court affirmed the central findings that U.S. District Court Judge Lewis A. Kaplan reached two years ago: absent the Thompson Memo (the Principles of Federal Prosecution of Business Organizations ("Principles") then-in-effect) and the actions of the U.S. Attorney's Office, KPMG would have paid the legal fees of all of its partners and employees without regard to cost. KPMG's decision not to advance legal fees "followed as a direct consequence of the government's overwhelming influence, and that KPMG's conduct therefore amounted to state action." The Court held that "the government thus unjustifiably interfered with defendants' relationship with counsel and their ability to mount a defense, in violation of the Sixth Amendment, and that the government did not cure the violation."

Foreshadowing the coming change in DOJ's policies regarding its evaluation of corporations in the course of criminal investigations, the Second Circuit made clear that it is fundamentally inappropriate for federal prosecutors to penalize companies for advancing legal fees to employees or for entering into other arrangements such as joint defense agreements.

That change to DOJ's policies – previewed by DOJ approximately six weeks ago (see our memo, [DOJ Seeks to Avoid Legislation by Adopting Revised Policies on Corporate Prosecutions](#), July 10, 2008) – was announced by Deputy Attorney General Mark Filip on the same day as the Second Circuit's decision. The revised Principles provide that:

- Credit for cooperation will not depend on whether a corporation has waived attorney-client privilege or work product protection, or produced materials protected by attorney-client or work product protections. It will depend on the disclosure of pertinent facts. The new policy also forbids prosecutors from asking for non-factual privileged information; indeed, DOJ's statement underscored that such material "lies at the core of the attorney-client privilege."
- Federal prosecutors are not to consider whether a corporation has advanced attorneys' fees to its employees, officers, or directors when evaluating cooperation. Under the earlier guidance, the Department reserved the right to consider such payments negatively in deciding whether to assign cooperation credit to a corporation.

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- Federal prosecutors may not consider whether the corporation has entered into a joint defense agreement in evaluating whether to give the corporation credit for cooperating.
- Federal prosecutors may not consider whether a corporation disciplined or terminated employees for the purpose of evaluating cooperation. Prosecutors may only consider whether a corporation has disciplined employees that the corporation identifies as culpable, and only for the purpose of evaluating the corporation's remedial measures or compliance program.

As noted in our earlier memo, the revised Principles appear to be part of an effort to avoid the passage of pending legislation aimed at limiting the ability of federal prosecutors to seek the production of materials protected by the attorney-client privilege or work product doctrine. On June 26, 2008, Senator Arlen Specter had re-introduced his bill, The Attorney-Client Privilege Protection Act of 2008, which would prohibit all federal investigators from requesting corporate waivers of privilege, thereby increasing the congressional pressure on DOJ. The Second Circuit's *Stein* opinion and the issuance of the revised Principles will undoubtedly be heralded as a victory for those business and advocacy groups who have long complained about DOJ's aggressive tactics in the investigation of corporate crime.

However, the Principles still identify a corporation's "timely and voluntary disclosure of wrongdoing" and its "cooperation" as factors relevant to the government's charging decision. And nothing about the revised Principles changes the long-established law that renders a corporation criminally liable for the acts of its employees performed within the scope of their employment and with the intent to benefit the corporation. As a result, corporations facing significant criminal investigations will still need to assess carefully how best to respond to such investigations, and may well still conclude that it is in the corporation's best interests to seek cooperation credit by providing relevant business records, identifying relevant personnel and evidence, and conveying other pertinent information to government investigators.

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