07-3042-cr

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

UNITED STATES OF AMERICA,

Appellant,

—against—

JEFFREY STEIN, JOHN LANNING, RICHARD SMITH, JEFFREY EISCHEID, PHILIP WIESNER, MARK WATSON, LARRY DELAP, STEVEN GREMMINGER, GREGG RITCHIE, RANDY BICKHAM, CAROL G. WARLEY, CARL HASTING, RICHARD ROSENTHAL,

Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF OF THE SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION AS *AMICUS CURIAE* IN SUPPORT OF DEFENDANTS-APPELLEES

IRA D. HAMMERMAN
KEVIN M. CARROLL
SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION
1101 New York Avenue NW
Washington, D.C. 20005
(202) 962-7382

MARK A. KIRSCH
KARA MORROW
TAMAR BRUGER
CLIFFORD CHANCE US LLP
31 West 52nd Street
New York, New York 10019
(212) 878-8000

STEPHEN M. NICKELSBURG
CLIFFORD CHANCE US LLP
2001 K Street NW
Washington, D.C. 20006
(202) 912-5000

Counsel for the Securities Industry and Financial Markets Association

RULE 26.1 CORPORATE DISCLOSURE STATEMENT

Amicus curiae the Securities Industry and Financial Markets Association is a non-profit corporation. It has no parent corporation, and no publicly held corporation owns 10% or more of its stock.

TABLE OF CONTENTS

RULE 26.1 CORPORATE DISCLOSURE STATEMENT......................................i

TABLE OF AUTHORITIES iii

PRELIMINARY STATEMENT 1

IDENTITY OF AMICUS CURIAE 3

STATEMENT OF INTEREST...4

SOURCE OF AUTHORITY 5

ARGUMENT 6

I. THE DISCRETION TO ADVANCE LEGAL FEES IS NECESSARY AND BENEFICIAL TO FIRMS, EMPLOYEES, AND THE MARKET 6

II. BECAUSE FINANCIAL INSTITUTIONS CANNOT AFFORD INDICTMENT, THE THOMPSON MEMORANDUM'S COOPERATION FACTORS WERE NOT "OPTIONAL"..........................16

CONCLUSION 19

TABLE OF AUTHORITIES

Page

Cases:

Homestore, Inc. v. Tafeen,
888 A.2d 204 (Del. 2005)..7, 8, 14

Kaung v. Cole Nat'l Corp,
884 A.2d 500 (Del. 2005)..7

United States v. Brown,
459 F.3d 509 (5th Cir. 2006),
cert. denied sub nom. Brown v. United States,
127 S. Ct. 2249 (2007) 14

United States v. Stein,
440 F. Supp. 2d 315 (S.D.N.Y. 2006)..18

United States v. Stein,
435 F. Supp. 2d 330 (S.D.N.Y. 2006)..4, 15

United States v. Stein,
495 F. Supp. 2d 390 (S.D.N.Y. 2007)..12, 13

VonFeldt v. Stifel Finance Corp.,
714 A.2d 79 (Del. 1998)..8

Statutes & Legislation:

8 Del. Code Ann. § 145(a)..13, 14

8 Del. Code Ann. § 145(e)..6, 13

6 Del. Code Ann. § 15-110..6

H.R. 3013, 110th Cong. § 3014(b)(2)(B) (2007) 3

Page

S. 186, 110th Cong. § 3014(b)(2)(B) (2007) 3

Other Authorities:

American Bar Ass'n Presidential Task Force on the Attorney-Client Privilege, Recommendation 302B (Aug. 2006), http://www.abanet.org/crimjust/policy/am06302b.pdf 15

R. FRANKLIN BALOTTI ET AL., DELAWARE LAW OF CORPORATIONS AND BUSINESS CORPORATIONS, § 4.22 (2007) 6, 7

BNA, *SEC Brought 656 Lawsuits in FY '07: Financial, Securities Firm Cases Top List,* SEC. L. DAILY, Nov. 16, 2007, http://pubs.bna.com/ip/bna/sld.nsf/eh/A0B5K0Q5Z7 12

Ken Brown, *et al.*, *Called to Account: Indictment of Andersen in Shredding Case Puts Its Future In Question*, WALL ST. J., Mar. 15, 2002 16

BOARD OF GOVERNORS FED. RES. SYS., 91ST ANNUAL REPORT 92-93 (2004), http://www.federalreserve.gov/boarddocs/rptcongress/annual04/ar04.pdf. 12

COMMITTEE ON CAPITAL MARKETS REGULATION, INTERIM REPORT (2006), http://www.capmktsreg.org/pdfs/11.30Committee_Interim_ReportREV2.pdf............... ....9, 16, 17, 18

Corporate Crime: Prosecutor's Dilemma, ECONOMIST, June 15, 2002 17

CORP. FRAUD TASK FORCE, SECOND YEAR REPORT TO THE PRESIDENT (2004), http://www.usdoj.gov/dag/cftf/2nd_yr_fraud_report.pdf............12

Jay A. Dubow, *Advancement and Indemnification for Officers in Securities Actions,* LEGAL INTELLIGENCER, Sept. 25, 2007 8

Page

Editorial, *Corporate Injustice*, WALL ST. J., Apr. 6, 2006, at A14……….. 17

Financial Industry Regulatory Authority, Five-Year Statistical Review 2002-2006, http://www.finra.org/PressRoom/Statistics/index.htm.................. 10

Financial Industry Regulatory Authority, FINRA Dispute Resolution Fact Sheet, http://www.finra.org/ArbitrationMediation/FINRADispute Resolution/FINRADisputeResolutionFactSheet/index.htm.....................12

James Glassman, *On the SEC Probe of NYSE "Specialist" Firms: Time Free the Stock Market to Make it More Competitive,* CAPITALISM MAGAZINE, May 4, 2003, http://www.capmag.com/article.asp?ID=2749..11

Joseph A. Grundfest, *Over Before It Started*, N.Y. TIMES, Jun. 14, 2005 14

MCKINSEY & CO., SUSTAINING NEW YORK'S AND THE U.S.' GLOBAL FINANCIAL SERVICES LEADERSHIP ("BLOOMBERG & SCHUMER REPORT") (2007) 9

Memorandum from Paul J. McNulty, Deputy Att'y Gen., U.S. Dep't of Justice, to All Component Heads and U.S. Att'ys, on Principles of Federal Prosecution of Business Organizations (Dec. 12, 2006), http://www.usdoj.gov/dag/speeches/2006/mcnulty_memo.pdf.................2

Memorandum from Larry Thompson, Deputy Att'y Gen., U.S. Dep't of Justice, to Heads of Dep't Components and U.S. Att'ys (Jan. 20, 2003), http://www.usdoj.gov/dag/cftf/corporate_guidelines.htm 2

ED MICHAELS ET AL., THE WAR FOR TALENT 2 (2001)....................................8

Liz Moyer, *Justice Beats A Retreat On Wall Street*, FORBES, Nov. 21, 2006, *available at* http://www.forbes.com/business/2006/11/21/specialists-wall-street-charges-biz-cx_lm_1121specialists.html 11

Liz Moyer, *NYSE Hits Specialist Brass*, FORBES, Feb. 6, 2007, *available at* http://www.forbes.com/business/2007/02/06/nyse-fleet-enforcement-biz-cx_lm_0206fleet.html 11

NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION, NASAA YEAR IN REVIEW 2006: ADVANCING A LEGACY OF INVESTOR PROTECTION, http://www.nasaa.org/content/Files/2006YIR.pdf 11

NYSE Exchange Hearing Panel Decision 04-127 (Aug. 11, 2004).............11

Dale A. Oesterle*, Early Observations on the Prosecutions of the Business Scandals of 2002-03: On Sideshow Prosecutions, Spitzer's Clash with Donaldson over Turf, the Choice of Civil or Criminal Actions, and the Tough Tactic of Coerced Cooperation,* 1 OHIO ST. J. CRIM. L. 443 (2004)...17, 18

Victor J. Rocco, Executives Do Not Need Waivers and Companies Should Not Offer Them: A Response to Mark Kressel, 116 YALE L.J. 262 (Supp. 2007) 7

John Roper, 4 Ex-Merrill Lynch Execs' Convictions Overturned, HOUSTON CHRONICLE, Aug. 2, 2006 14

Kara Scannell, *Moving the Market*, WALL ST. J., Jun. 13, 2005...................17

Donald W. Searles & Jay L. Pomerantz, *United States: DOJ Revises Policy On Demanding Waiver of Attorney-Client Privilege*, MONDAQ BUS. BRIEFING, Jan. 2, 2007, *available at* 2007 WLNR 188013 8

Page

SEC, 2008 CONGRESSIONAL JUSTIFICATION, http://www.sec.gov/about/secfy08congbudgjust.pdf 11

SEC, 2007 PERFORMANCE & ACCOUNTABILITY REPORT, http://www.sec.gov/about/secpar/secpar2006.pdf................................... 12

SEC, 2006 PERFORMANCE & ACCOUNTABILITY REPORT, http://www.sec.gov/about/secpar/secpar2006.pdf................................... 12

SEC, 2005 PERFORMANCE & ACCOUNTABILITY REPORT, http://www.sec.gov/about/secpar/secpar2005.pdf................................... 12

SECURITIES INDUSTRY ASS'N, THE COSTS OF COMPLIANCE IN THE U.S. SECURITIES INDUSTRY (2006), http://www.sifma.org/research/surveys/pdf/CostofComplianceSurveyReport.pdf 10

Stephen Taub, *KPMG, DOJ in "High-Wire Negotiations,"* CFO.com, Jun. 17, 2005, http://www.cfo.com/article.cfm/4096271?f=search 17

Testimony before Subcomm. on Capital Markets, Insurance and Govt. Sponsored Enterprises: Before the Comm. On Financial Services, U.S. House of Reps (2005) (statement of Linda Fienberg, President of NASD Dispute Resolution), http://www.finra.org/PressRoom/SpeechesTestimony/LindaFienberg/P013652.. 10

The Thompson Memorandum's Effect on the Right to Counsel in Corporate Investigations: Hearing before the United States Senate Committee on the Judiciary (2006) (testimony of Hon. Edwin Meese III), available at http://judiciary.senate.gov/testimony.cfm?id=2054&wit_id=5741 18

United States Gov't Accountability Office, Report to Congressional Committees, *Financial Regulation: Industry Trends Continue to Challenge the Federal Regulatory Structure* (Oct. 2007).......................... 9

RODMAN WARD JR. ET AL., FOLK ON DELAWARE GENERAL CORPORATION LAW § 145 (2001) 7

Joseph Weber, *The Heavy Hand of Justice*, BUS. WK., Apr. 1, 2002 17

The Woes of KPMG, ECONOMIST, Jun. 25, 2005 17

Douglas R. Young, *Shifting Boundaries – As Courts Reexamine Cooperation In Federal Investigations, Individuals Are Fighting Back*, MONDAQ BUS. BRIEFING, Oct. 25, 2006, *available at* 2006 WLNR 18644071 6

PRELIMINARY STATEMENT

The Securities Industry and Financial Markets Association ("SIFMA") submits this brief as *amicus curiae* to address the principles supporting the common practice of companies advancing attorneys' fees to their officers, directors, and employees.

The government's now-repudiated policy of taking a firm's advancement of attorneys' fees into account in deciding whether the firm adequately cooperated with a criminal investigation was improper and ill-advised. The policy wrongfully interfered with employees' lawful access to independent legal advice, as the District Court held and defendants-appellees ably demonstrate. It also unwisely undermined employers' well-established right to advance fees to individuals who face legal jeopardy as a result of doing their jobs.

The discretion to advance legal fees to officers, directors, and employees is particularly important in the heavily-regulated securities and financial industry. Indemnification of employees and advancement of their fees are essential to recruiting and retaining top talent and to aligning employees' interests with those of their firms. The practice of fee advancement is affirmatively sanctioned under the laws of every state, and is frequently the subject of specific terms of individual employment contracts. Nonetheless, the government's criteria for corporate prosecutions treated fee advancement with extreme suspicion — indeed, as cause

to conclude that a firm was not cooperating and deserved to be indicted.[1] Because indictment means death for a financial services firm, this policy forced companies to terminate or strictly condition their practice of advancing fees.

This interference with the lawful and long-standing relationships between firms and their employees was exceedingly bad policy, undertaken principally to separate individuals from their preferred counsel early in an investigation. There is no legitimate reason for this tactic. The mere advancement of fees is not obstruction or the protection of wrongdoers — it can be extremely difficult to determine whether an employee under investigation has acted wrongfully, particularly in the early stages of a complex proceeding. Tellingly, the government retreated from its policy in 2006, and now takes the position that "[p]rosecutors generally should *not* take into account whether a corporation is advancing attorneys' fees to employees or agents under investigation and indictment."[2] And

---

[1] Memorandum from Larry Thompson, Deputy Att'y Gen., U.S. Dep't of Justice, to Heads of Dep't Components and U.S. Att'ys (Jan. 20, 2003) ("Thompson Memorandum"), *available at* http://www.usdoj.gov/dag/cftf/corporate_guidelines. *htm*.

[2] Memorandum from Paul J. McNulty, Deputy Att'y Gen., U.S. Dep't of Justice, to All Component Heads and U.S. Att'ys, on Principles of Federal Prosecution of Business Organizations (Dec. 12, 2006) ("McNulty Memorandum") *available at* http://www.usdoj.gov/dag/speeches/2006/mcnulty_memo.pdf (emphasis added). The government's current policy is to take the advancement of fees into account only in "extremely rare cases," in which "the totality of the circumstances show that it was intended to impede a criminal investigation." *Id.*

Congress is considering legislation to ban the practice entirely.[3] Although these recent developments are positive, it is unclear whether they will endure. Thus, it remains fundamentally important that this Court affirm the judgment of the District Court and hold that the government's conduct in this case was impermissible under established law.

IDENTITY OF AMICUS CURIAE

SIFMA brings together the shared interests of more than 650 securities firms, banks, and asset managers that have a vital interest in the outcome of this appeal. These institutions are the gateway to the U.S. capital markets, linking thousands of companies to millions of investors. Among other things, they underwrite equity and debt offerings for domestic and foreign issuers, broker securities trades, provide financial advisory services, publish analysis, lend money to companies ranging from small start-ups to the Fortune 100, and make private-equity investments in large and small companies. In short, these financial institutions are essential to every aspect of the global capital markets' function.

---

[3] *See* H.R. 3013, 110th Cong. § 3014(b)(2)(B) (2007) (as passed by the House, Nov. 13, 2007) ("In any Federal investigation or criminal or civil enforcement matter, an agent or attorney of the United States shall not . . . condition a civil or criminal charging decision . . . on, or use as a factor in determining whether an organization . . . is cooperating with the Government . . . the provision of counsel to, or contribution to the legal defense fees or expenses of, an employee of that organization."); S. 186, 110th Cong. § 3014(b)(2)(B) (2007).

SIFMA's mission is to promote policies and practices that expand and perfect markets, foster the development of new products and services, and create efficiencies for member firms, while preserving and enhancing the public's trust and confidence in the markets and the industry. SIFMA works to represent its members' interests locally and globally through offices in New York, Washington, D.C., and its associated firm, the Asia Securities Industry and Financial Markets Association, in Hong Kong.

STATEMENT OF INTEREST

A fundamental underpinning of the District Court's decision is the precept that firms lawfully and appropriately may — and often do — advance legal fees to employees caught up in litigation or government investigations as a result of their employment.[4] This certainly is true for financial institutions, which operate in one of the most heavily regulated industries in the world and which regularly fund legal representation for their employees and agents.

SIFMA has an interest in preserving the lawful relationships among its members and their officers, directors, and employees, including by protecting firms' discretion to advance their legal fees under appropriate circumstances.

---

[4] *See United States v. Stein*, 435 F. Supp. 2d 330, 361 (S.D.N.Y. 2006) ("[T]he only question now before the Court is whether a criminal defendant has a right to obtain and use in order to prepare a defense *resources lawfully available to him or her*, free of knowing or reckless government interference.") (emphasis added).

Federal prosecution policy as established in the Thompson Memorandum and dramatically exemplified by the facts of this case severely undermined that discretion. Indeed, as a result of the Thompson Memorandum and individual prosecutors' actions, firms under investigation — including KPMG — were forced to abandon or modify their fee advancement practices, to the detriment of their relationships with their agents. The District Court properly recognized that the Thompson Memorandum went too far, damaging not only the individuals involved but also these beneficial business arrangements. SIFMA has a substantial interest in righting this balance and restoring the relationships that have long served its members, the markets, and the economy.

SOURCE OF AUTHORITY

SIFMA has sought leave of the Court to file this brief. Defendants-Appellees consent to the motion. Appellant takes no position with respect to the motion.

ARGUMENT

I. THE DISCRETION TO ADVANCE LEGAL FEES IS NECESSARY AND BENEFICIAL TO FIRMS, EMPLOYEES, AND THE MARKET

Agreements to indemnify and advance legal fees to officers, directors, and employees are ubiquitous among U.S. companies. All fifty states have adopted laws that permit firms to provide such financial support.[5] For example, the Delaware General Corporation Law expressly authorizes the advancement of legal expenses to officers and directors under certain circumstances.[6] And the articles of incorporation or bylaws of forty-eight of the fifty largest U.S. corporations include indemnification and fee advancement provisions.[7] These laws and corporate policies reflect the considered judgment that firms and markets benefit when

---

[5] Douglas R. Young, *Shifting Boundaries – As Courts Reexamine Cooperation In Federal Investigations, Individuals Are Fighting Back*, MONDAQ BUS. BRIEFING, Oct. 25, 2006, available at 2006 WLNR 18644071.

[6] 8 Del. Code Ann. § 145(e). "More than twenty states follow the Delaware statute's organization and content and five other states have statutes very similar to that of Delaware." R. FRANKLIN BALOTTI ET AL., DELAWARE LAW OF CORPORATIONS AND BUSINESS ORGANIZATIONS, § 4.22 n.418 (2007). The Delaware Revised Uniform Partnership Act includes a similar provision. 6 Del. Code Ann. § 15-110 (2006).

[7] *See* Young, *supra* note 5.

individuals acting within the scope of their employment do not fear individual liability for their professional activities.[8]

By mitigating the fear of liability for legal expenses arising out of one's employment, fee advancement aligns the interests of individuals and their firms and ensures better decisionmaking. Providing security from individual liability fosters an environment in which leaders and employees can take legitimate risks with confidence, which promotes initiative and encourages innovation.[9] Fee advancement thus benefits firms and their shareholders as much as it benefits individuals, and has been recognized as "a desirable mechanism to manage risk in return for greater corporate benefits."[10]

---

[8] *See generally* BALOTTI ET AL., *supra* note 6, § 4.22; RODMAN WARD JR. ET AL., FOLK ON DELAWARE GENERAL CORPORATION LAW § 145 (2001).

[9] *See* Victor J. Rocco, *Executives Do Not Need Waivers and Companies Should Not Offer Them: A Response to Mark Kressel*, 116 YALE L.J. 262, 263 (Supp. 2007) (observing that "executives . . . have ample financial incentive to take bold actions for the corporation's benefit, undeterred by potential liability" in part because of fee advancement policies).

[10] *Kaung v. Cole Nat'l. Corp*, 884 A.2d 500, 509 (Del. 2005) (noting that the individual benefits from indemnification and fee advancement are secondary to the benefits to the company); *see also Homestore, Inc. v. Tafeen*, 888 A.2d 204, 218 (Del. 2005) ("Although advancement provides an individual benefit to corporate officials, it is actually a desirable underwriting of risk by the corporation in anticipation of greater corporate-wide rewards for its shareholders.") (internal citations omitted).

Fee advancement also enables companies to attract and retain talent — the lifeblood of the firm.[11] Individuals in sophisticated industries are keenly aware of the potential for personal liability for corporate decisions, as well as the role of indemnification and fee advancement in limiting that potential. Fee advancement thus "encourag[es] capable women and men to serve as corporate directors and officers, secure in the knowledge that the corporation will absorb the costs of defending their honesty and integrity."[12] Senior executives in particular view indemnification and advancement policies as critical in deciding whether to join a firm, and frequently bargain to include express indemnification and advancement provisions in their contracts.[13] Thus, indemnification and fee advancement are essential to attracting and retaining executives willing to take appropriate risks[14] —

---

[11] *See* ED MICHAELS ET AL., THE WAR FOR TALENT 2 (2001) ("[T]alent is now a critical driver of corporate performance and . . . a company's ability to attract, develop, and retain talent will be a major competitive advantage far into the future.").

[12] *VonFeldt v. Stifel Fin. Corp.*, 714 A.2d 79, 84 (Del. 1998); *see also Homestore*, 888 A.2d at 218.

[13] Jay A. Dubow, *Advancement and Indemnification for Officers in Securities Actions,* LEGAL INTELLIGENCER, Sept. 25, 2007.

[14] *See Homestore*, 888 A.2d at 218; *VonFeldt*, 714 A.2d at 84; Donald Searles, *DOJ Revises Policy On Demanding Waiver of Attorney-Client Privilege*, MONDAQ BUS. BRIEFING, Jan. 2, 2007, available at 2007 WLNR 188013 (stating that fee advancement and indemnification "promote corporate goodwill, and thereby attract and retain high-quality employees, officers and directors").

which is in turn critical to corporate performance and potentially the survival of the firm.

Fee advancement also can be a matter of basic fairness to employees — especially in industries such as financial services, which face extensive and strict regulatory oversight. "The United States has the toughest administrative enforcement of securities laws in the world."[15] Moreover, "the [financial regulatory] system is complex, with a single large firm subject to oversight by multiple federal and state agencies," as well as self-regulatory organizations ("SROs") and the enforcement arms of individual exchanges.[16] As a result, regulatory inquiries and investigations are an everyday part of the financial

---

[15] COMMITTEE ON CAPITAL MARKETS REGULATION, INTERIM REPORT 11 (2006), http://www.capmktsreg.org/pdfs/11.30Committee_Interim_ReportREV2.pdf.

[16] United States Gov't Accountability Office, Report to Congressional Committees, *Financial Regulation: Industry Trends Continue to Challenge the Federal Regulatory Structure*, at 77-78 (Oct. 2007); *see also* MCKINSEY & CO., SUSTAINING NEW YORK'S AND THE U.S.' GLOBAL FINANCIAL SERVICES LEADERSHIP 77-78 ("BLOOMBERG & SCHUMER REPORT") (2007). Financial institutions may be subject to the oversight of the Securities and Exchange Commission ("SEC"), Commodity Futures Trading Commission ("CFTC"), the Federal Energy Regulatory Commission ("FERC"), the Federal Deposit Insurance Corporation, the Federal Reserve, the Office of Thrift Supervision, the Office of Foreign Assets Control of the U.S. Department of the Treasury, the Financial Industry Regulatory Authority ("FINRA") and other SROs, state regulators such as insurance regulators and licensing boards, and the enforcement arms of individual securities exchanges.

business.[17] These inquiries regularly focus not only on firms, but also on individual employees, their supervisors, and their managers.

Regulatory inquiries are relatively easy to trigger. For example, for broker-dealers and investment advisors, regulatory inquiries and enforcement proceedings may begin with a simple investor complaint. And these complaints occur with some frequency. FINRA,[18] which regulates approximately 5,000 member firms and 675,000 registered representatives, received an average of 5,000 investor complaints annually from 2002 through 2006.[19] In 2004, the NASD administered over 9,000 arbitrations and 2,000 mediations — which are other barometers of investor complaints.[20] The North American Securities Administrators Association,

---

[17] In 2004, for example, securities firms spent approximately $23.2 billion on compliance-related activities. *See* SECURITIES INDUSTRY ASS'N, THE COSTS OF COMPLIANCE IN THE U.S. SECURITIES INDUSTRY 3 (2006), http://www.sifma.org/research/surveys/pdf/CostofComplianceSurveyReport.pdf.

[18] FINRA was formed in July 2007 through the consolidation of NASD and the member regulation, enforcement and arbitration functions of the New York Stock Exchange. FINRA performs market regulation under contract for the NASDAQ Stock Market, the American Stock Exchange, the International Securities Exchange and the Chicago Climate Exchange.

[19]FINRA, Five-Year Statistical Review 2002-2006, http://www.finra.org/PressRoom/Statistics/index.htm.

[20] *Testimony before Subcomm. on Capital Markets, Insurance and Govt. Sponsored Enterprises: Before the Comm. On Financial Services, U.S. House of Reps* (2005) (statement of Linda Fienberg, President of NASD Dispute Resolution), available at http://www.finra.org/PressRoom/SpeechesTestimony/LindaFienberg/P013652; *see also* FINRA Dispute Resolution Fact Sheet,

which is comprised of state and local securities regulators, reports that state securities regulators brought 3,635 enforcement actions of their own in 2004-2005.[21]

Individual complaints in turn may lead to complex, parallel enforcement proceedings.[22] Or enforcement agencies may initiate enforcement cases on their own.[23] The SEC initiated over 900 investigations and filed over 600 civil and

---

http://www.finra.org/ArbitrationMediation/FINRADisputeResolution/FINRADisputeResolutionFactSheet/index.htm.

[21] NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION (NASAA), NASAA YEAR IN REVIEW: 2006: ADVANCING A LEGACY OF INVESTOR PROTECTION, http://www.nasaa.org/content/Files/2006YIR.pdf.

[22] SEC, 2008 CONGRESSIONAL JUSTIFICATION, http://www.sec.gov/about/secfy08congbudgjust.pdf (observing that investor complaints are a source of SEC enforcement actions and that the SEC works with the Justice Department to support criminal prosecutions of alleged securities fraud).

[23] For example, the NYSE opened an investigation of certain specialists for alleged fraudulent trading practices in 2003. *See NYSE Exchange Hearing Panel Decision 04-127*, at 2 (Aug. 11, 2004). These investigations led the SEC and the Justice Department to begin their own investigations. *See* James Glassman, *On the SEC Probe of NYSE "Specialist" Firms: Time Free the Stock Market to Make it More Competitive,* CAPITALISM MAGAZINE May 4, 2003, available at http://www.capmag.com/article.asp?ID=2749 (reporting that the NYSE actions prompted an SEC investigation); *see also* Liz Moyer, *NYSE Hits Specialist Brass* FORBES (Feb. 6, 2007), available at http://www.forbes.com/business/2007/02/06/nyse-fleet-enforcement-biz-cx_lm_0206fleet.html (reporting that fifteen specialists were singled out in an NYSE probe, "which eventually made its way to the U.S. Attorney's office"). Ultimately, the U.S. Attorney dropped charges against five of the specialists, two cases were dismissed and two ended in acquittals. Liz Moyer, *Justice Beats A Retreat On Wall Street*, FORBES, Nov. 21, 2006, available at

administrative proceedings in each of 2005, 2006, and 2007.[24] The Justice Department charged over 900 defendants with corporate fraud crimes in connection with over 400 filed cases between 2002 and 2004.[25] Other financial regulators also pursue active enforcement programs.[26]

Given these active and overlapping regulatory and enforcement regimes, financial firms simply must have the discretion to advance fees to employees caught up in government inquiries. Indeed, qualified personnel would likely forego employment opportunities in this industry knowing that a simple complaint could lead to ruinous legal bills[27] — or that they could lose their representation if a

---

http://www.forbes.com/business/2006/11/21/specialists-wall-street-charges-biz-cx_lm_1121specialists.html.

[24] SEC, 2007 PERFORMANCE & ACCOUNTABILITY REPORT, http://www.sec.gov/about/secpar/secpar2007.pdf; SEC, 2006 PERFORMANCE & ACCOUNTABILITY REPORT, http://www.sec.gov/about/secpar/secpar2006.pdf; SEC, 2005 PERFORMANCE & ACCOUNTABILITY REPORT, http://www.sec.gov/about/secpar/secpar2005.pdf; *see also* BNA, *SEC Brought 656 Lawsuits in FY '07, Financial, Securities Firm Cases Top List*, SEC. L. DAILY, Nov. 16, 2007 http://pubs.bna.com/ip/bna/sld.nsf/eh/A0B5K0Q5Z7.

[25] CORPORATE FRAUD TASK FORCE, SECOND YEAR REPORT TO THE PRESIDENT (July 20, 2004), http://www.usdoj.gov/dag/cftf/2nd_yr_fraud_report.pdf.

[26] *Id.* (reporting on the CFTC and FERC); BOARD OF GOVERNORS FED. RES. SYS., 91ST ANNUAL REPORT 92-93 (2004), http://www.federalreserve.gov/boarddocs/rptcongress/annual04/ar04.pdf.

[27] The high cost of defending complex white collar cases is well known. Defense attorneys in this case estimated that the total costs for legal services would fall between $7 million and $24 million per individual. *See United States v. Stein*, 495

regulatory matter attracts a prosecutor's interest. To be sure, in some cases employees violate the rules and deserve to be sanctioned. But the subjects of investigations often are vindicated, with the help of qualified legal representation supplied by their firms.

Determining which employees should receive representation and which should not thus can be extraordinarily difficult, especially in the early stages of a proceeding. For this reason, laws and corporate policies give firms the discretion to advance fees at any time through the final disposition of a case. Under the Delaware statute, for example, firms have the discretion to advance an officer's or director's expenses "in defending any civil, criminal, administrative or investigative action, suit or proceeding," at any time "in advance of [its] final disposition," so long as he agrees to repay the firm if he is ultimately found to be ineligible for indemnification.[28] The mere fact that an employee becomes the

---

F. Supp. 2d 390, 424 (S.D.N.Y. 2007). Even in smaller securities fraud and other financial cases, defense costs can reach from tens to hundreds of thousands of dollars. *See, e.g., id.* (observing that "one of the defendants' attorneys submitted a declaration stating the actual cost of his defense of a much smaller white collar criminal case involving a much shorter trial and far fewer documents than this one was $3.3 million").

[28] 8 Del. Code Ann. § 145(e). An individual is eligible for indemnification "if [he] acted in good faith and in a manner [he] reasonably believed to be in or not opposed to the best interests of the corporation, and, with respect to any criminal action or proceeding, had no reasonable cause to believe [his] conduct was unlawful." *Id.* § 145(a). Fee advancement fills the gap between allegation and the

target of a civil or criminal investigation, or even is indicted, thus does not mean that he is ineligible for fee advancement. Under the Delaware standard, even a conviction does not create a presumption of ineligibility.[29] This standard makes sense — as convictions may be overturned.[30]

By forcing companies to deny fee advancement to employees the prosecutors deem "culpable" at the outset of an investigation, the Thompson Memorandum shifted fee eligibility determinations to the beginning of legal proceedings, and from corporate counsel to prosecutors. There is "no realistic choice" but to cooperate fully with the government in its culpability assessment, "even if evidence might later demonstrate that the government's theories were legally infirm or that factual allegations couldn't withstand cross-examination."[31]

---

ultimate determination of the right to indemnification, providing "immediate interim relief from the personal out-of-pocket financial burden of paying the significant on-going expenses inevitably involved with investigations and legal proceedings." *Homestore, Inc*., 888 A.2d at 211.

[29] 8 Del. Code Ann. § 145(a) (stating that a conviction "shall not, of itself, create a presumption that the person" lacked "reasonable cause to believe that [his] conduct was unlawful").

[30] *See, e.g., United States v. Brown,* 459 F.3d 509 (5th Cir. 2006), *cert. denied sub nom*, *Brown v. United States*, 127 S. Ct. 2249 (2007) (reversing wire fraud convictions and conspiracy charges against four former Merrill Lynch executives previously convicted for their alleged role in Enron transactions); *see also* John Roper, *4 ex-Merrill Lynch Execs' Convictions Overturned*, HOUS. CHRON. (Aug. 2, 2006) (reporting on the exonerated executives' release).

[31] Joseph A. Grundfest, *Over Before It Started*, N.Y. TIMES, June 14, 2005, at A23.

This thwarting of, and improper interference with, the bargain between employer and employee served no legitimate purpose, but sought only to separate individuals from their preferred counsel early in the investigation.

Accelerating and usurping the fee advancement decision has a severe and pernicious effect on individuals and their organizations. There is no basis for the government to conclude that the mere advancement of fees suggests a lack of cooperation or obstruction of justice. Simply put, fee advancement is not obstruction — it is necessary to a defense. Defending white collar and enforcement investigations requires costly, specialized representation. Without an employer's assistance, financing a representation in even a simple regulatory inquiry would drain the resources of all but the most well-compensated employees. Even if an individual has sufficient resources to retain *a* lawyer, it is "difficult if not impossible" to finance a defense in a complex securities or white-collar enforcement case.[32] "[B]ecause the cost of defending complex criminal prosecutions is so severe, a decision not to advance attorneys' fees effectively forces capitulation of individuals to prosecutorial demands, irrespective of guilt or

---

[32] American Bar Ass'n Presidential Task Force on the Attorney-Client Privilege, Recommendation 302B (Aug. 2006), http://www.abanet.org/crimjust/policy/am06302b.pdf.; *see also Stein*, 435 F. Supp. 2d at 338 (noting the expense of retaining an attorney "with the skills, business sophistication, and resources that are important to able representation" in complex business litigation); *see also supra* n.28.

innocence."[33] Although this may serve the prosecution's narrowest tactical aims, it does not serve the interests of truth-seeking or justice. In short, there is no legitimate reason to remove the traditional and beneficial discretion of the firm.

II. BECAUSE FINANCIAL INSTITUTIONS CANNOT AFFORD INDICTMENT, THE THOMPSON MEMORANDUM'S COOPERATION FACTORS WERE NOT "OPTIONAL"

The government has contended that its policies did not interfere with companies' discretion to advance fees, because fee advancement was only one factor in the indictment calculus and companies remained free to advance fees if they chose.[34] At best, this argument demonstrates profound naiveté regarding the *in terrorem* effect of a potential indictment on corporate defendants. More disturbing, it appears to reflect a lack of responsibility for the power prosecutors wield during the pre-indictment stage of a criminal case.

"In the 212-year history of the U.S. financial markets, no major financial services firm has ever survived an indictment."[35] Indeed, an indictment is widely understood to be a catastrophe for a financial institution, because "the market will

---

[33] COMMITTEE ON CAPITAL MARKETS REGULATION, *supra* note 15, at 85.

[34] *See, e.g.,* Gov. Br. at 105-06 ("To the extent that KPMG, because of its own assessment of its culpability and desire to appear cooperative, chose to condition legal fee payments on cooperation and terminate them upon indictment, that decision was its own.").

[35] Ken Brown, *et al.*, *Called to Account: Indictment of Andersen in Shredding Case Puts Its Future In Question*, WALL ST. J., Mar. 15, 2002, at A1.

convict and sentence an indicted financial services firm long before a court is able to do so."[36] For example, the press has extensively documented the evaporation of Arthur Andersen as a result of its indictment, presenting a stark lesson for the financial services community.[37]

For this reason, "as a practical matter, only a rare CEO will risk the death sentence that a corporate indictment represents," and "'cooperation' as defined by [the Department of] Justice is hardly optional."[38] Under such circumstances, "[t]otal capitulation . . . may be the only real business strategy left to save a

---

[36] COMMITTEE ON CAPITAL MARKETS REGULATION, *supra* note 15, at 84; *see also* Dale A. Oesterle, *Early Observations on the Prosecutions of Business Scandals of 2002-03: On Sideshow Prosecutions, Spitzer's Clash with Donaldson over Turf, the Choice of Civil or Criminal Actions, and the Tough Tactic of Coerced Cooperation*, 1 OHIO ST. J. CRIM. L. 443, 471-72 (2004) ("In business, particularly in the financial services industry . . . an indictment can ruin a firm, or a career, well before trial.").

[37] *See, e.g., Corporate Crime: Prosecutor's Dilemma,* ECONOMIST, June 15, 2002 ("For a financial firm, or indeed any other business that operates under the scrutiny of regulators, an indictment can be a death warrant."); Kara Scannell, *Moving the Market*, WALL ST. J., June 13, 2005, at C3 (noting that, like Arthur Andersen, financial firms E. F. Hutton and Drexel Burnham and Lambert Inc. collapsed after being indicted and observing "few companies — particularly in the financial-services industry — could survive criminal charges or a guilty plea"); Joseph Weber, *The Heavy Hand of Justice*, BUS. WK., Apr. 1, 2002, at 32 (reporting that Andersen's collapse was assured after the failure of settlement talks with the Justice Department); *The Woes of KPMG*, ECONOMIST, Jun. 25, 2005 (observing that an indictment would amount to a death sentence for KPMG); Stephen Taub, *KPMG, DOJ in "High-Wire Negotiations,"* CFO.com, Jun. 17, 2005.

[38] Editorial, *Corporate Injustice*, WALL ST. J., Apr. 6, 2006, at A14.

financial firm's future" and protect the interests of shareholders and employees.[39] As a result, "[c]ompanies reasonably consider[ed] each of the Thompson Memorandum factors to be mandatory" — and, in the view of one former Attorney General, "corporate counsel would [have been] irresponsible to advise their clients otherwise."[40]

It is fanciful to suggest that companies would continue to advance fees notwithstanding the risk that a prosecutor would view fee advancement as noncooperation — whether or not the companies believed their personnel were culpable.[41] That is why "KPMG did everything it could 'to be able to say at the right time and with the right audience, we're in full compliance with the Thompson Memorandum.'"[42] In short, the District Court's decision accurately reflects the incentives that a financial firm faces as a result of a government investigation.

---

[39] Oesterle, *supra* note 36, at 475.

[40] *The Thompson Memorandum's Effect on the Right to Counsel in Corporate Investigations: Hearing before the United States Senate Committee on the Judiciary* (2006) (testimony of Hon. Edwin Meese III), available at http://judiciary.senate.gov/testimony.cfm?id=2054&wit_id=5741

[41] COMMITTEE ON CAPITAL MARKETS REGULATION, *supra* note 15, at 84-85.

[42] *United States v. Stein*, 440 F. Supp. 2d 315, 319 (S.D.N.Y. 2006).

CONCLUSION

The Thompson Memorandum and prosecutors' actions unjustifiably and perniciously interfered with a bedrock feature of corporate governance and employer/employee relationships. For the foregoing reasons, this Court should affirm the judgment of the District Court.

Dated: January 22, 2008

Respectfully submitted,

/s/ Mark A. Kirsch

Mark A. Kirsch
Kara Morrow
Tamar Bruger
CLIFFORD CHANCE US LLP
31 West 52nd Street
New York, NY 10019
(212) 878-8000

Stephen M. Nickelsburg
CLIFFORD CHANCE US LLP
2001 K Street NW
Washington, DC 20006
(202) 912-5000

Ira D. Hammerman
Kevin M. Carroll
SECURITIES INDUSTRY AND
FINANCIAL MARKETS ASSOCIATION
1101 New York Avenue NW
Washington, DC 20005
(202) 962-7382

Counsel for the Securities Industry and Financial Markets Association

CERTIFICATE OF COMPLIANCE WITH RULES 29(d) AND 32(a)

1. This brief complies with Fed. R. App. P. 29(d) and Fed. R. App. P. 32(a)(7)(B) because this brief contains 2458 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

2. This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in Microsoft Word 97 in 14 point Times New Roman font.

/s/ Kara Morrow
Kara Morrow
CLIFFORD CHANCE US LLP
31 West 52nd Street
New York, NY 10019
(212) 878-8000

Counsel for the Securities Industry and Financial Markets Association

ANTI-VIRUS CERTIFICATION

Case Name: United States v. Stein

Docket Number: 07-3042-cr

I, Jacqueline Gordon, hereby certify that the Amicus Brief submitted in PDF form as an e-mail attachment to **briefs@ca2.uscourts.gov** in the above referenced case, was scanned using CA Software Anti-Virus Release 8.3.02 (with updated virus definition file as of 1/22/2008) and found to be VIRUS FREE.

/s/ Jacqueline Gordon
Jacqueline Gordon
Record Press, Inc.

Dated: January 22, 2008