Legal Backgrounder

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2009 Massachusetts Avenue, NW
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202.588.0302 wlf.org

Efforts to Expose Corporate Monitors' Reports Underscore Need to Carefully Design Deferred Prosecution Agreements

by Carol Elder Bruce and Alexandra Marinzel

In the last several years, two federal circuit courts have reversed trial judges' attempts to second-guess pretrial diversion agreements between federal prosecutors and the targets of criminal charges. Most recently, the U.S. Court of Appeals for the Second Circuit reversed a district court decision to unseal a monitor's report in a criminal case where HSBC Holdings plc and HSBC Bank, USA, N.A. (collectively, HSBC) were under a monitor's review pursuant to the terms of a 2012 deferred prosecution agreement (DPA or Agreement) between HSBC and the Department of Justice (DOJ). *United States v. HSBC Bank USA, N.A.*, 863 F.3d 125 (2d Cir. 2017) (*HSBC*). The court's ruling, rooted in separation-of-powers principles, has ongoing implications for white-collar criminal defendants and the parameters of federal prosecutors' authority.

Deferred Prosecution Agreements

DPAs are part of a significant DOJ pretrial diversion program designed to resolve corporate criminal cases short of indictment. The threat of charges is not merely hypothetical—the government actually files its charges against the company in a formal complaint (with the company's consent) and agrees in the simultaneously filed DPA to defer those charges as long as the company complies with all the terms of the Agreement. Separately, the parties also file a joint motion with the court to extend Speedy Trial Act deadlines during the deferred prosecution period. A DPA's terms focus on the steps necessary to remediate past criminal conduct and ensure best practices in compliance going forward, with the ultimate goal of obtaining a dismissal of the pending criminal case.

DPAs frequently include a requirement that the corporation hire an independent monitor (approved by the government) to observe and report on the company's efforts to comply with the Agreement. The government reviews the monitor's reports but retains the unilateral discretion to determine whether the company has satisfied the terms of the DPA. If the compliance satisfies the terms of the DPA to the government's satisfaction, the government will voluntarily dismisses the pending charges with prejudice at the completion of the DPA period.

Monitorships have been criticized for a lack of transparency in the selection process, for excessive implementation costs, and for having an overreaching scope and intrusiveness when dealing with defendant companies.[1] The appointment of former Attorney General John Ashcroft to a monitor position by then-

[1] *See*, *e.g.*, Alex J. Brackett and Katherine Mims Crocker, *The Past, Present, and Uncertain Future of Corporate Monitors*, Washington Legal Foundation Working Paper, July 2017, http://www.wlf.org/upload/legalstudies/workingpaper/07-14-2017_BrackettCrockerWP.pdf.

Carol Elder Bruce is a Shareholder, and **Alexandra Marinzel** is an Associate, with Murphy & McGonigle, PC in the firm's Washington, DC office. Both practice primarily in the White Collar Defense, Investigations, and Compliance Counseling practice. Carol Elder Bruce serves on Washington Legal Foundation's Legal Policy Advisory Board.

U.S. Attorney for the District of New Jersey Chris Christie in 2007 was so widely criticized that DOJ issued internal guidelines, known as the Morford Memo,[2] in response. The Morford memo set forth nine principles governing the selection, scope of duties, independence, and responsibilities of the monitor. The Morford Memo was later supplemented by a second internal DOJ guidance memo, the Grindler Memo, which presented a tenth principle dealing with DOJ's role in resolving disputes between the monitor and defendant corporations.[3]

***HSBC* Background**

In December 2012, after a four-year investigation, the United States entered into a five-year DPA with HSBC, deferring criminal charges predicated on anti-money laundering and Office of Foreign Asset Control sanctions violations. The alleged internal compliance weaknesses allowed Columbian and Mexican drug dealers to launder over $881 million through HSBC. In exchange for the government's agreement to refrain from prosecution, HSBC forfeited $1.256 billion, and agreed to pay $665 million in civil penalties. HSBC also agreed to improve its anti-money laundering and compliance programs, among other things. In order to ensure HSBC upheld its end of the bargain, particularly with respect to developing the internal controls it promised, the DPA provided for the appointment of an independent monitor to evaluate HSBC and prepare periodic reports over a five-year period.

With their DPA in hand, HSBC and DOJ sought court approval of an exemption from the Speedy Trial Act's requirement that a criminal case proceed to trial within 70 days after charges are filed. Such approval is routinely granted by courts to effectuate the parties' agreement that the government will defer prosecution while the defendant demonstrates good conduct. For HSBC, the story took an unusual turn when the district court conditioned its approval of the DPA on the court's own "continued monitoring of its execution and implementation." Specifically, the district court demanded that it receive quarterly status reports from the parties, and eventually demanded that it receive the monitor's annual reports as well. Effectively, the court *sua sponte* appointed itself to monitor the independent monitor.

A member of the public sought to access the first confidential monitor's report after it was submitted under seal. Over objections of both the government and HSBC, the court made the extraordinary decision to make public the monitor's report, albeit with redactions. This disclosure risked the exposure of sensitive, internal operations and weaknesses that HSBC, with the monitor's oversight, was seeking to remedy—information that competitors and others might seek to exploit.

HSBC and the government appealed the district court's ruling to the Second Circuit. The court reversed the district court's decision, making it plain that neither the district court's general supervisory powers, nor the Speedy Trial Act's procedural requirement that courts "approve" trial date postponements, invite a district court to insert itself into the substantive review or implementation of the DPA. By meddling in the monitoring of the DPA, the district court "impermissibly encroached on the Executive's constitutional mandate to 'take Care that the Laws be faithfully executed'" under Article II of the U.S. Constitution.

As the Second Circuit explained, DOJ is entitled to a "presumption of regularity," meaning that courts must presume that DOJ is "lawfully discharging its duties." In HSBC's case, the district court took the

[2] U.S. Dep't of Justice, Office of the Deputy Attorney General, *Selection and Use of Monitors in Deferred Prosecution Agreements and Non-Prosecution Agreements with Corporations*, Mar. 7, 2008, https://www.justice.gov/sites/default/files/dag/legacy/2008/03/20/morford-useofmonitorsmemo-03072008.pdf.

[3] U.S. Dep't of Justice, Office of the Acting Deputy Attorney General, *Additional Guidance on the Use of Monitors in Deferred Prosecution Agreements and Non-Prosecution Agreements with Corporations*, May 25, 2010, https://www.justice.gov/usam/criminal-resource-manual-166-additional-guidance-use-monitors-dpas-and-npas.

opposite view—it hypothesized that prosecutors might abuse their power, and thus the court preemptively sought to monitor the situation. Yet the district court's concern over potential misconduct lacked any connection to HSBC's case—in other words, the presumption of regularity had not been challenged, let alone rebutted.

The Second Circuit left open the possibility that district court intervention may be warranted where there are indicia of Executive Branch misconduct or abuse of power. Absent being alerted to such circumstances—by a whistleblower letter, for example—the Second Circuit made it clear that the court has no authority to preemptively monitor the DPA's implementation in order to police theoretical misconduct.

Judge Pooler agreed with the majority's decision, but wrote separately to suggest that it is time for Congress to weigh in with legislation that would offer courts a role in the monitoring and implementation of DPAs. In Judge Pooler's view, the ever-expanding use of DPAs for corporate defendants is concerning and warrants additional oversight in a realm where prosecutors are currently subject to none. Under the current approach to such arrangements, Judge Pooler wrote, the prosecution "retains sole discretion to decide if the corporation adequately complied with the [DPA], allowing the prosecution to act as prosecutor, jury, and judge." In doing so, the prosecution has the freedom to "enforce legal theories without such theories ever being tested in a court proceeding." In any event, though, Judge Pooler recognized that the courts are powerless to change this state of affairs.

Future Implications for DPAs and Monitors

HSBC highlights the discomfort some district courts experience with the current DPA process and their limited authority to do anything about it—an issue that previously arose in *United States v. Fokker Services B.V.*, 818 F.3d 733, 738 (D.C. Cir. 2016). In *Fokker*, the D.C. Circuit similarly determined that a district court was out of line when it refused to extend the time to prosecute under the Speedy Trial Act after scrutinizing the terms of a DPA. In the district court's view, the DPA was far too lenient, or "grossly disproportionate to the gravity" of the offending behavior. The D.C. Circuit vacated, holding that the district court lacks authority to weigh in on the government's charging decisions. Other courts will likely recognize the soundness of the Second Circuit's and D.C. Circuit's decisions. Absent the legislation called for by Judge Pooler, DOJ remains governed only by internal guidelines and prosecutorial discretion.

By making clear that the court cannot *sua sponte* manage the DPA monitoring process, *HSBC* helps preserve the confidentiality of independent monitor reports, a crucial aspect of DPAs' effectiveness . However, it remains to be seen whether third parties may find other avenues to obtain access to these reports, such as the Freedom of Information Act requests at issue in a pending motion in *100Reporters LLC v. United States Department of Justice*, No. 14-cv-01264 (D.D.C.).

DOJ and defendant companies should take steps to protect the confidentiality of monitor reports and the underlying documentation by carefully delineating the monitor's role to specifically address the alleged conduct, and by developing protocols to govern the monitor's access to confidential information. For example, the parties could require that the monitor review certain confidential information in person. DOJ, defendant companies, and monitors also need to carefully safeguard the confidentiality of any resulting monitor report. Of course, despite the best efforts of the parties to keep the monitor's report confidential in *HSBC,* the court insisted on receiving a copy, thus creating the circumstances that led to the unsealing order.

Finally, another way to avoid potential disclosure problems is to use a different pre-trial diversion vehicle. DOJ could employ a Non-Prosecution Agreement (NPA) instead of a DPA in appropriate cases.

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While DPAs are filed in court and are subject to the requirements of the Speedy Trial Act, NPAs are agreements between the government and the defendant that do not invoke the court's jurisdiction, unless the implementation of the NPA (with or without a monitor) fails. Like DPAs, NPAs resolve white collar matters quickly and efficiently, help companies avoid collateral consequences of criminal indictments, and avoid consequences to innocent third parties, such as shareholders and employees.

HSBC is a reminder that independent monitors conduct their duties without judicial supervision. The case drives home the importance of retaining an experienced and independent attorney who is sensitive to the confidentiality needs of the corporation as well as the implications of non-compliance. The monitor must be skilled at quickly assessing a DPA's requirements and the corporation's remedial obligations as he or she recommends meaningful changes aimed at creating a more robust corporate compliance program and culture.

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