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White Collar Watch

The Newsletter of the White Collar and Government Enforcement Practice

Saul Ewing LLP

White Collar and Government Enforcement Practice

Contents

Eleventh Circuit Holds that Production of Foreign Bank Account Records May be Compelled in Criminal Investigation Under Required Records Exception to Fifth Amendment Privilege

By Nicholas J. Nastasi and Matthew J. Smith

The Eleventh Circuit recently joined the Fifth, Seventh, and Ninth Circuits in holding that subpoenaed foreign financial records properly fall within the Required Records Exception to the Fifth Amendment privilege against self-incrimination, and their production may thus be compelled in a criminal investigation. *In re Grand Jury Proceedings, No. 4-10*, No. 12-13131, 2013 WL 452768 (11th Cir. Feb. 7, 2013).

The case arose from a grand jury investigation involving the suspected failure of a husband (the "Target" of the investigation) and wife: (1) to disclose their ownership of or income derived from foreign bank accounts, held both together and individually, on their jointly-filed tax returns; and (2) to file, with the U.S. Department of the Treasury, the required Reports of Foreign Bank and Financial Accounts ("FBAR") forms for the alleged accounts. The investigation was jointly conducted by the Internal Revenue Service ("IRS"), the U.S. Department of Justice Tax Division, and the U.S. Attorney's Office.

During the investigation, the government served subpoenas on both the Target and his wife seeking production of "any foreign financial account records that they were required to keep pursuant to the federal regulations governing offshore banking" for the period 2006 to present. The couple refused to produce the subpoenaed records, and the government filed a motion to compel in the District Court. In its motion, the government argued that, pursuant to the Bank Secrecy Act ("BSA"), 31 U.S.C. § 5311 *et seq.*, and its implementing regulations, the Target and his wife were required to maintain the foreign financial account records. The government contended, therefore, that the Required Records Exception to the Fifth Amendment privilege against self-incrimination applied, and the couple could not withhold the records on Fifth Amendment grounds. The District Court agreed and granted the motion to compel.

On appeal to the Eleventh Circuit, the couple argued that the Required Records Exception did not apply to the subpoenaed records and that their Fifth Amendment privilege against self-incrimination should preclude compulsion of the records. In its February 7, 2013 ruling, the Circuit Court held that the records properly fell under the Required Records Exception and, accordingly, affirmed the District Court's order granting the government's motion to compel production.

The Fifth Amendment provides that "[n]o person … shall be compelled in any criminal case to be a witness against himself … ." This provision applies when an accused is compelled to make an incriminating "testimonial communication," which may include the act of producing evidence in response to a subpoena as well as to the evidence itself. However, this protection is not absolute. As the Eleventh Circuit observed in this case, "when the government is authorized to regulate an activity, an individual's Fifth Amendment privilege does not prevent the government from imposing recordkeeping, inspection, and reporting requirements as part of a valid regulatory scheme." Under the Required Records Exception, the government may mandate the retention or inspection of records created under such a regulatory scheme.

In assessing whether the Required Records Exception applied to the subpoenaed foreign financial records in this case, the Circuit Court observed that the Supreme Court has developed three "premises" for the application of the exception. In order for the exception to apply: (1) the purpose of the government's inquiry must be "*essentially regulatory;*" (2) the records must be of a kind which the regulated party has "c*ustomarily kept;*" and (3) the records must assume "*public aspects*" which render them at least analogous to public documents. With this analytical framework in mind, the Court addressed each premise individually.

First, the Court ruled that the purpose of the record-keeping requirements of the BSA was "essentially regulatory" in nature. The Court rejected the Target's argument that the purpose of the BSA was not "essentially regulatory" because the Act was intended to aid law enforcement in criminal matters rather than regulatory matters. The Court concluded that "the BSA has multiple purposes," and the fact that a statute "relates both to criminal law and to civil regulatory matters does not strip the statute of its status as 'essentially regulatory.'" The Court reasoned that, because there is nothing inherently illegal about having a foreign bank account, the record-keeping requirements of the BSA were "essentially regulatory in nature, as they do not target inherently illegal activity or a group of persons inherently suspect of criminal activity."

Next, the Court ruled that the records sought were of the type "customarily kept" in connection with the regulated activity. The Court agreed with the Ninth and Fifth Circuits that the information required to be kept under the regulations was "basic account information" that bank customers would customarily keep, partly because customers must report it to the IRS each year, and partly because they simply need that information to access their accounts.

Third, the Court ruled that the requested records satisfied the final premise in that they assume a "public aspect" which renders them at least analogous to public documents. Specifically, the Court observed that, where personal information is compelled subject to a valid regulatory scheme, that information assumes a public aspect. The Court concluded that, because the BSA is a valid regulatory regime, the information sought pursuant to the Act therefore "assumes a public aspect."

Finally, the Court rejected the Target's "attempt to draw a distinction, for Fifth Amendment privilege purposes, between his act of producing the records and the records themselves." Although either the act of producing records or the records themselves could be testimonial and incriminating, the Court agreed with the Seventh Circuit's rationale that "the government or a regulatory agency should have the means, over an assertion of the Fifth Amendment Privilege, to inspect the records it requires an individual to keep as a condition of voluntarily participating in that regulated activity." Moreover, the Court reasoned that the "voluntary choice" to engage in an activity with record-keeping requirements under a valid regulatory scheme "carries consequences," including "the possibility that those records might have to be turned over upon demand."

In a growing number of jurisdictions, the Required Records Exception to the Fifth Amendment's privilege against self-incrimination is being applied to compel individuals to produce foreign financial account records, despite the potentially incriminating and testimonial nature of those communications. Although the regulations requiring the maintenance of such records are allegedly "regulatory," those regulations, in conjunction with the Required Record Exception, clearly serve a significant role in aiding government enforcement in criminal investigations. Notably, the requirements of the BSA extend beyond foreign accounts, and certain domestic transactions could potentially be subject to production as well.

Supreme Court Holds SEC to Five-Year Statute of Limitations for Civil Enforcement Actions; Decision May Extend to Other Federal Agencies

By Christopher R. Hall and Brian P. Simons

The Supreme Court recently rebuffed an attempt by the U.S. Securities and Exchange Commission ("SEC") to gain more time to file actions to enforce civil penalties by invoking the "discovery rule." In the case of *Gabelli vs. SEC*, the Court reasoned that this rule does not apply unilaterally to the SEC because it is a "different kind of plaintiff" who has access to tools that should allow the agency to commence an enforcement action within five years of the allegedly wrongful conduct occurring.

The opinion will come as welcome relief to individuals and businesses facing action not only by the SEC but other government agencies. Decisions from several Circuit Courts of Appeal have – until now – allowed the Internal Revenue Service ("IRS") to avoid the five-year statue of limitations imposed by 28 U.S.C § 2462. Relying on the discovery rule, the IRS has pursued fraud cases under 26 U.S.C. §§6700 and 6701 up to five years after the agency discovered the allegedly wrongful acts, even if the acts had occurred more than five years before the cases were filed. The Supreme Court decision calls this practice into question.

Gabelli involved SEC allegations of a market timing scheme that violated the Securities Exchange Act of 1934 and the Investment Advisers Act of 1940. The SEC had instituted a civil action against Marc Gabelli, the portfolio manager for the Gabelli Global Growth Fund ("GGGF"), a mutual fund, and Bruce Alpert, chief operating officer of Gabelli Funds (an investment advisor to GGGF) more than five years after the alleged conduct.

This penalty action was governed by § 2462, a general statute of limitations applicable to civil government actions to enforce statutes that do not specify a period of repose. It provides that "an action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise, shall not be entertained unless commenced within five years from the date when the claim first accrued." The Second Circuit Court of Appeals held that the government's claim did not "accrue" until either the SEC discovered the violation, or could have discovered it with reasonable diligence, relying on the discovery rule, which staves off the accrual of a claim in certain cases involving fraud. The Supreme Court, however, disagreed. (For an analysis of the oral argument, view the story at this link, http://www.saul.com/publications-alerts-1002.html, where we reported that based on the tenor of the argument, the Court was poised to likely rule as it did).

The Supreme Court noted that the discovery rule offers relief from the strictures of the limitations period for initiating suit in cases of fraud where a plaintiff may have been deprived of "even knowing that he or she has been defrauded." This permits the aggrieved to seek recompense for the injury. The government, however, is "a different kind of plaintiff," the Court observed, and seeks "a different kind of relief" in a penalty case. The Court noted that the SEC's very purpose is to root out fraud, and it is equipped with a variety of tools for identifying it, including whistleblower incentives, "cooperation agreements" with violators in exchange for information and required inspections of books and records. These are tools unavailable to the average litigant.

Rather than seeking recompense for an injury, penalty actions seek to punish, further distinguishing these actions from those in which the discovery rule applies. The Court did take care to leave the discovery rule available to the government when it could properly be characterized as a fraud victim seeking recompense, citing *Exploration Co. v. United States*. In *Exploration*, a foreign corporation had fraudulently obtained coal-mining land in Colorado which had been part of the public domain of the United States, and the government was able to invoke the discovery rule in a suit seeking to reverse the land transfers. The Gabelli Court distinguished cases like that from those in which the government seeks a civil penalty.

The Court's ruling in *Gabelli* has implications for all penalty actions governed by § 2462. Of particular note are actions prosecuted by the IRS under § 6700, which imposes a penalty for promoting abusive tax shelters, and § 6701, which penalizes the aiding and abetting of understatements of tax liability. In language tracking that of the discovery rule, the Fifth Circuit had determined in *Sage v. United States* that § 6700 is subject to no limitations period. The Second and Eighth Circuits have also found § 6700 unaffected by § 2462. The Sixth Circuit has regarded § 6701 as unbounded by a statute of limitations.

The rationale of *Gabelli* opens the door to challenging the validity of prior decisions that allowed the government to invoke the discovery rule in civil penalty cases, including not only SEC enforcement actions, but also IRS actions. The government's inability to ward off the "accrual" of a claim for statute of limitations purposes provides a ready counterpoint to any attempt to invoke the discovery rule in such actions.

The D.C. Circuit Expands the Scope of Honest-Services Fraud and Illegal-Gratuities Prosecutions in *Ring v. United States*

By Christopher R. Hall and Brett S. Covington

Summary

The U.S. Court of Appeals for the D.C. Circuit in *United States v. Ring* recently upheld a conviction under the public sector "honest-services" fraud statute and the "illegal-gratuities" statute. Notably, the court: (1) expanded the definition of "corrupt payments" for purposes of the honest-services fraud statute; and (2) expanded the definition of "official action" for purposes of the illegal-gratuities statute.

Based upon *Ring,* lobbyists will need to be particularly careful when providing gifts (other than campaign contributions) to public officials, as those gifts may be viewed as a form of bribery. In addition, all persons (regardless of whether they are lobbyists) will need to be particularly careful when sending gifts to government employees in exchange for favors (expediting a visa application). Former government employees — now part of the "revolving door" — will need to be particularly careful in not seeking favors from current government employees, as those practices may be viewed as an illegal gratuity.

Background

The defendant, Kevin Ring, was a former lobbyist and associate of Jack Abramoff. While his primary activities involved campaign fundraising, Ring also treated public officials to dinners, travel, concerts, and other forms of entertainment.

In 2010, Ring was convicted on three counts of honest-services fraud, one count of paying an illegal gratuity, and one count of conspiracy to pay an illegal gratuity. During trial, the government offered evidence that Ring had provided meals, tickets, and travel to public officials, which were linked to official acts that benefited Ring and his clients. After Ring was sentenced to 20 months in prison, he challenged his conviction on appeal.

Honest-Services Fraud

The honest-services statute criminalizes "a scheme or artifice to deprive another of the intangible right of honest services." 18 U.S.C. §1346. The landmark Enron scandal decision, *Skilling v. United States*, 130 S. Ct. 2896 (2010), clarified the doctrine as applied in § 1346. In order to avoid a finding of unconstitutional vagueness, the Supreme Court in *Skilling* limited the scope of the honest-services fraud statute to bribery and kickback schemes, as opposed to "undisclosed self-dealing by a public official or private employee."

Ring was prosecuted under a bribery theory of honest-services fraud. This meant that the government needed to prove the elements of bribery, 18 U.S.C. §201(b)(1), in order to convict Ring of honest-services fraud. That is, the government needed to prove that Ring gave gifts with the "intent" to "influence an official act" by way of a corrupt *quid pro quo*. The District Court in Ring instructed the jury that the government did not have to show that the *quid pro quo* was explicit, or even that the public officials had accepted Ring's gifts, in order to prove bribery.

Ring's trial arose just a few months after the Supreme Court's decision in *Skilling*. On appeal, Ring argued that the District Court's jury instructions were flawed to the extent that the court instructed that an implicit *quid pro quo* was sufficient to prove bribery and that the public official did not need to accept the gift.

The D.C. Circuit upheld the District Court's instructions, holding that the government met its burden of proof by establishing the existence of an implicit *quid pro quo* when the "thing of value" being offered was something **other** than a campaign contribution. First, the court recognized that because campaign contributions implicate First Amendment concerns, the government must establish an explicit *quid pro quo* to support a conviction under the honest-services statute. Second, the court recognized that when a lobbyist offers "things of value," other than campaign contributions, such as hockey tickets, the First Amendment interest is "de minimis," and therefore does not require the government to prove an explicit *quid pro quo* to prove bribery. In other words, when a lobbyist offers "things of value" other than campaign contributions, the government can establish bribery, and therefore a violation of the honest-services fraud statute, without establishing an explicit agreement between the lobbyist and the public official.

In addition, the D.C. Circuit held that the government did not need to prove that the public official accepted the implicit *quid pro quo* — that is, the gift — in order to prove that the lobbyist violated the honest-services fraud statute. The D.C. Circuit reasoned that bribery does not require an explicit agreement between the parties, or the actual acceptance of the bribe by the offeree (in this case, the pubic official). The crime of bribery was complete as soon as Ring offered the gift to the public official with the intent to receive an official act in return.

Illegal-Gratuity Statute

The illegal-gratuity statute makes it unlawful to "give[], offer[], or promise[] anything of value to any public official . . . for or because of any official act." 18 U.S.C. § 201(c). Ring was charged with paying an illegal gratuity when he gave Washington Wizards basketball tickets to an attorney at the Justice Department's Intergovernmental Affairs Office as a reward for helping to expedite review of a visa application for a foreign student seeking to attend a private school. Upon receiving the request, the DOJ attorney forwarded Ring's email to another DOJ official who recommended that he contact U.S. Citizenship and Immigration Services (USCIS). The DOJ attorney called a USCIS official's secretary and urged her to expedite the application, and forwarded Ring's email to the secretary along with a personal note. The secretary then passed the email along to five different USCIS officials in an effort to "make sure . . . action was being taken to answer the request." Within a single business day, the USCIS agreed to expedite the visa application.

After learning that the DOJ attorney's efforts had been successful, Ring sent Abramoff an email reporting that the attorney had "[h]elped on the school and [was] now looking for tickets" to two Washington Wizards basketball games. The DOJ attorney received the tickets, which were paid for by Abramoff.

On appeal, Ring did not dispute that he provided the tickets "for or because of" the DOJ attorney's assistance with the visa application. Rather, Ring argued that the government failed to offer sufficient evidence that the attorney took an "official action" within the meaning of the illegal-gratuity statute. Specifically, Ring argued that the DOJ attorney's forwarding of the email did not constitute an "official act" because the DOJ attorney lacked decisionmaking authority with respect to visa applications. Ring argued that the forwarding of the email was nothing more than an "informational inquiry," and therefore did not qualify as an "official act."

The D.C. Circuit rejected Ring's argument, and held that a rational jury could have found that the DOJ attorney's efforts to expedite the visa application qualified as "official action." The court noted that the DOJ attorney was a member of the Intergovernmental Affairs Office, and therefore part of his job was to reach "across agency boundaries to get things done." The court also held that even though the DOJ attorney did not have ultimate decisionmaking authority regarding the visa application, he nonetheless "influenced" the visa application process, and therefore a rational jury could have concluded that the attorney engaged in "official action."

There are two key takeaways from *Ring.* First, lobbyists must be particularly careful when providing gifts (other than campaign contributions) to public officials, as those acts could be viewed as an implicit *quid pro quo* and give rise to honest-services fraud. Because the government no longer has to establish an explicit agreement between the lobbyist and public official, the burden of proof on the government is significantly lower. This decision should have a major impact on the lobbying industry, as it will constrain lobbyists from engaging in activities that were previously lawful.

Second, this decision makes clear that everyone (even apart from lobbyists) needs to be careful when seeking favors from government employees, as those favors may be viewed as "illegal gratuities" if gifts (such as basketball tickets) are involved. Even if a government employee does not have decisionmaking authority over a particular request, the fact that he or she can "influence" the decision may suggest that the government employee engaged in "official action." Former government employees, now in the private workplace, should be particularly careful when seeking favors from current government employees. Even though there is a "revolving door" between the government and the private workplace, appearances do matter, and former government employees should be especially careful when seeking favors from their old friends and contacts.

On March 11, 2013, Kevin Ring petitioned the D.C. Circuit asking that the case be reheard by the full Circuit. The instant decision was by a unanimous three-judge panel of the D.C. Circuit. If the D.C. Circuit denies the *en banc review,* then Ring may petition the U.S. Supreme Court for review.

Court Upholds Executive's Conviction Stemming from Off-Label Drug Promotion

By Christopher R. Hall and Gregory G. Schwab

The U.S. Court of Appeals for the Ninth Circuit has upheld the wire fraud and misbranding convictions and sentence of InterMune Inc. founder W. Scott Harkonen. *United States v. Harkonen*, No. 11-10209 (9th Cir. March 4, 2013). That decision, while based on different circumstances than the landmark decision by the Second Circuit in *Caronia* (which we have written about in this story, http://www.saul.com/publications-alerts-1021.html), creates further tension between lawful promotional marketing and criminal off-label practices.

Harkonen was indicted in 2008 on charges of wire fraud and misbranding under the Food, Drug, and Cosmetic Act ("FDCA") for creating and disseminating a press release that promoted off-label uses for the drug Actimmune. A federal jury in September 2009 found him guilty of wire fraud for the press release but acquitted him of misbranding under the FDCA. Harkonen was sentenced in April 2011 to three years' probation and was ordered to pay a $20,000 fine. The government had sought a $1 million fine and 10 years' imprisonment. He subsequently appealed to the Ninth Circuit.

Harkonen was the first chief executive officer tried for off-label promotion. He argued on appeal that a scientific debate over whether a given treatment causes a particular effect is speech protected by the First Amendment and falls outside the scope of the mail and wire fraud laws. The Ninth Circuit dismissed this characterization as an assertion of innocence. "[G]enuine debates of any sort are, by definition, not fraudulent. Here, a jury found, beyond a reasonable doubt, that Harkonen issued the Press Release with the specific intent to defraud, and that finding is supported by the evidence presented at trial." The Court also rejected Harkonen's due process argument as "essentially a redressing" of his First Amendment claim.

Harkonen's counsel has stated publicly that he will ask the Ninth Circuit for *en banc* review.

On the surface, the Ninth Circuit's decision does not appear to raise any complicated freedom of speech issues. The First Amendment does not protect from prosecution harmful, dangerous or fraudulent speech. However, the mail and wire fraud statutes give prosecutors wide latitude to investigate and prosecute disfavored speech. The term "to defraud" in the statutes includes any sort of "dishonest method or scheme" and any "trick, deceit, chicane or overreaching." And, according to the Ninth Circuit in *Harkonen*, statements are fraudulent if "misleading or deceptive" and need not be "literally false."

The line between lawful promotion and misleading or deceptive statements is not always bright. Pharmaceutical and medical device manufacturers will want to stand clear of the gray area in between to ensure that their promotional efforts receive the protection afforded to truthful commercial speech by the Second Circuit in *Caronia* and the Supreme Court in *Sorrell v. IMS Health*, 131 S.Ct. 2653 (2011). In short, strong compliance policies and programs to ensure truthful promotional statements have never been more important.

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