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White Collar Crime Report™

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SUPREME COURT

Two attorneys at Skadden, Arps, Slate, Meagher & Flom LLP examine the cases involving white collar criminal and civil enforcement matters decided by the U.S. Supreme Court during its October 2016 term. The authors also discuss cases the high court will decide during its current term and the potential impact on practitioners.

White Collar Cases at the U.S. Supreme Court

BY JOCELYN STRAUBER AND DANIEL WEINSTEIN

This article examines U.S. Supreme Court decisions from the October 2016 term involving white collar criminal and civil enforcement matters, such as bank fraud, insider trading, forfeiture, disgorgement, bribery, double jeopardy, federal criminal procedure, and the federal sentencing guidelines. The Court's decisions in all cases were closely tied to the statutory or constitutional text at issue, and the relevant precedent, with outcomes that sometimes favored the government and sometimes favored the defense. We take a look at those decisions here, as well as those cases in the white collar enforcement area that the Court will take up in the October 2017 term and potentially in the terms thereafter.

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Disgorgement

Kokesh v. SEC

Four years ago, the Court made clear that the five-year statute of limitations set forth in 28 U.S.C. § 2462—which applies to any ''action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise''—applies to actions in which the Securities and Exchange Commission seeks monetary penalties. *See Gabelli v. SEC*, 568 U.S. __, 133 S. Ct. 1216, 1224 (2013) (unanimously holding that the five-year clock begins to tick when the conduct occurred, not when it is discovered). However, the remedy of disgorgement is not explicitly identified in Section 2462. In *Kokesh*, the Court unanimously held that disgorgement is a penalty, such that the five-year statute of limitations in Section 2462 applies when disgorgement is sought for violations of federal securities laws.

Charles Kokesh was found to have misappropriated nearly $35 million between 1995 and 2009 from two investment-advisory firms he owned and was ordered to pay a $2.4 million penalty, consistent with *Gabelli*, for conduct within the five-year limitations period. The district court also ordered disgorgement of nearly $35 million plus interest, an amount arising primarily from conduct preceding the five-year limitations period. The U.S. Court of Appeals for the Tenth Circuit, siding with the D.C. Circuit and First Circuit in a split with the Eleventh Circuit, affirmed the district court and held that

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the five-year limitation in Section 2462 did not apply because disgorgement was not a penalty.

In an opinion by Justice Sonia Sotomayor, the Supreme Court reversed, finding disgorgement in the securities-enforcement context to be a ''penalty'' within the meaning of Section 2462, and therefore subject to the five-year statute of limitations. The Court disagreed with the SEC's contention that disgorgement is merely an equitable remedy that restores the status quo, reasoning that disgorgement is a penalty because it is imposed for violating public laws and for punitive purposes, and often it is not merely compensatory, given that disgorged funds can be paid to the U.S. Treasury, not to victims.

In SEC investigations that span lengthy time periods, such as Foreign Corrupt Practices Act investigations, *Kokesh* may significantly limit the SEC's ability to seek disgorgement in the absence of a tolling agreement. Given the significant disgorgement amounts collected by the SEC in the past for conduct beyond the five-year statute of limitations, this decision may cause the SEC to reassess its investigative priorities.

The *Kokesh* decision further suggests that the Court may be open to a future challenge to the SEC's ability to collect disgorgement in the first instance, expressing concern that no statute authorizes the SEC to do so, and noting that the opinion should not be interpreted as addressing whether courts possess authority to order disgorgement in SEC enforcement proceedings. In light of the Supreme Court's invitation, we expect practitioners to press this issue in future cases.

Forfeiture

Honeycutt v. United States

Honeycutt addressed joint and several liability in the context of criminal forfeiture pursuant to 21 U.S.C. § 853, which mandates forfeiture of ''any property constituting, or derived from, any proceeds . . . obtained, directly or indirectly, as the result of'' certain drug crimes. In a unanimous opinion authored by Justice Sotomayor, the Court found that joint and several liability is not permitted under Section 853(a)(1), and held that a defendant may not be held jointly and severally liable for property that a co-conspirator derived from the crime but that the defendant did not acquire. That is, the government may not seek to forfeit property from a defendant that was obtained by that defendant's co-conspirator.

Terry Honeycutt, a hardware store employee, was convicted post-trial of conspiracy to distribute narcotics, in connection with his sale of a water purification product commonly used to manufacture methamphetamine. His brother Tony, the store owner, pleaded guilty and agreed to forfeit a portion of the profits from the sales. But Terry in fact had not received any such profits, therefore the district court declined to order forfeiture, ruling that Terry was not jointly liable with Tony for profits Terry never obtained. The Sixth Circuit reversed, and the Supreme Court granted certiorari to resolve a circuit split on the issue. The Supreme Court reversed the Sixth Circuit, finding that there is no joint and several liability for forfeiture among members of a criminal conspiracy, unless the individual conspirator acquired or personally benefited from the forfeitable property.

The Court's decision was based on the text of the forfeiture statute, which limits forfeiture to tainted property, and the statutory framework, which the Court concluded was inconsistent with joint and several liability. But while the statute at issue only addresses forfeiture within the context of the Controlled Substances Act, the Court's reasoning arguably may extend to other forfeiture contexts as well, including provisions of the general civil and criminal forfeiture statutes, 18 U.S.C. §§ 981-982, which apply to property that was ''obtained, directly or indirectly'' from an offense. Indeed, the Supreme Court subsequently vacated a forfeiture judgment in a mortgage fraud case pursuant to 18 U.S.C. § 982 and directed the Third Circuit to revisit the issue in light of *Honeycutt*. *See Brown v. United States*, No. 16-7794, 582 U.S. ___ (June 12, 2017) (order granting cert., vacating judgment and remanding). Given this similar statutory language, and particularly in light of the Supreme Court's focus on what the plain text of the statute authorizes, cases involving similarly worded forfeiture statutes—such as the general civil and criminal forfeiture statutes discussed above, 18 U.S.C. §§ 981-982, as well as the RICO criminal forfeiture statute, 18 U.S.C. § 1963—may arguably warrant a similar outcome, and we would not be surprised to see counsel advance such a theory in upcoming cases.

Insider Trading

Salman v. United States

In *Salman*, the Court's first insider trading law decision in nearly 20 years, the Court unanimously held that an insider ''tipper'' breaches a fiduciary duty by disclosing confidential information as a gift to a trading relative or friend, affirming the Ninth Circuit's decision. In doing so, the Court foreclosed an alternate approach to insider trading liability adopted by the Second Circuit in the *United States v. Newman* case. *See United States v. Newman*, 773 F.3d 438, 452 (2d Cir. 2014).

Bassam Salman was convicted of insider trading, in violation of Section 10(b) of the Securities Exchange Act of 1934 and related SEC regulations (codified at 15 U.S.C. § 78j) after he received lucrative trading tips from an extended family member who in turn had received the information from another family member. Salman argued that he could not be held liable as a tippee because the tipper did not personally receive money or property in exchange for the tips and thus did not personally benefit from them. In 2014, in the *Newman* case, the Second Circuit had expanded the elements of tippee liability, requiring ''proof of a meaningfully close personal relationship'' between tipper and tippee ''that generates an exchange that is objective, consequential, and represents at least a potential gain of a pecuniary or similarly valuable nature.'' The Ninth Circuit disagreed with the Second Circuit and did not require similar proof of potential gain. Instead, it relied on the Supreme Court's 1983 decision in *Dirks v. SEC*, which stated, without qualification, that the tipper receives a sufficient personal benefit by making ''a gift of confidential information to a trading relative or friend.''

In an opinion by Justice Samuel A. Alito Jr., the Supreme Court held in *Salman* that the Ninth Circuit properly applied *Dirks* in holding that a tipper benefits personally upon giving a gift of trading information to a relative or friend. Addressing the additional requirement the Second Circuit articulated in *Newman* that the

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tipper must also receive something of a pecuniary or similarly valuable nature in exchange for a gift to family or friends, the Court clarified that such a requirement is inconsistent with *Dirks*. By reaffirming *Dirks* as binding precedent, the Court clarified that tippers may not provide inside information as gifts to trading relatives or friends, notwithstanding the Second Circuit's noteworthy efforts in *Newman* to exclude such cases from the reach of insider trading laws. Indeed, the Second Circuit recently recognized that ''logic of *Salman* abrogated *Newman*'s 'meaningfully close personal relationship' requirement.'' *United States v. Martoma*, 869 F.3d 58, 61 (2d Cir. 2017).

While hailed as a victory for prosecutors and SEC officials pursuing insider trading cases, the *Salman* decision is a limited one. While it does reject *Newman's* additional requirement that the insider receive something of a pecuniary or similarly valuable nature in exchange, it leaves for another day more difficult questions, including:

- what constitutes a sufficiently close friendship to fall within the *Dirks* rule,
- what establishes a personal benefit to the insider in cases that fall outside that rule, and
- the level of knowledge that must be proven with respect to remote tippees who are more removed from the corporate insiders than the defendant in this case.

Bank Fraud

Shaw v. United States

In *Shaw*, the Court unanimously held that the fraudulent wiring of funds out of a bank customer's account is sufficient under the federal bank fraud statute to sustain a conviction for defrauding a financial institution.

The petitioner, Lawrence Shaw, was convicted of bank fraud after he fraudulently transferred funds from a bank account belonging to an acquaintance to accounts at other institutions through which Shaw was able to obtain the funds. Shaw was convicted of violating 18 U.S.C. § 1344, and the Ninth Circuit affirmed his conviction.

Shaw argued that diverting funds from a bank customer's account did not constitute defrauding the bank itself, on the theory that the bank suffered no pecuniary loss. But the Court disagreed, and in an opinion by Justice Stephen G. Breyer, the Court in *Shaw* agreed with the Ninth Circuit and held that the bank had a cognizable property interest in its customer's account, such as the right to use the funds as a source of loans, from which the bank can profit, sufficient to trigger culpability under Section 1344, even where the bank was not the intended victim of the fraud and where the bank did not suffer any financial loss.

While the ruling appears to effect a marginal expansion of the scope of the bank fraud statute, it may lead prosecutors to bring bank fraud charges in a wider variety of white collar cases as a way to take advantage of a broader statute of limitations and enhanced criminal penalties. *See* 18 U.S.C. § 3293. Particularly given the government's increased reliance on criminal resolutions in enforcement actions, it would not be surprising to see renewed attention to the bank fraud statute in the wake of *Shaw*, including efforts to prosecute additional white collar cases as bank fraud.

Bribery and Double Jeopardy

Bravo-Fernandez v. United States

In *Bravo-Fernandez*, the Court unanimously held that the issue-preclusion component of the Double Jeopardy Clause does not bar the government from retrying defendants after a jury has returned inconsistent verdicts of conviction on some counts and acquittal on others, where the convictions have been vacated for instructional error unrelated to the inconsistency.

Prosecutors charged Juan Bravo-Fernandez, an entrepreneur, with paying a bribe to Hector Martinez-Maldonado, then a senator serving the Commonwealth of Puerto Rico, in the form of an all-expenses paid trip to Las Vegas, allegedly to secure Martinez-Maldonado's help in passing legislation that would have provided substantial financial benefits to Bravo-Fernandez's enterprise. Martinez-Maldonado submitted and supported the legislation in the Puerto Rican Senate prior to the Las Vegas trip, and soon after he returned, Martinez-Maldonado voted to enact the legislation.

Based on these events, a jury in Puerto Rico convicted Bravo-Fernandez and Martinez-Maldonado of bribery, in violation of 18 U.S.C. § 666, but acquitted them of conspiracy to violate Section 666, under 18 U.S.C. § 371, and traveling in interstate commerce to further violations of Section 666, under 18 U.S.C. § 1952(a)(3)(A). The First Circuit vacated the Section 666 convictions for instructional error. It stated that while the evidence at trial sufficed to support a guilty verdict, the erroneous charge was not necessarily harmless, and vacated the Section 666 convictions and remanded for further proceedings.

It is well-settled that defendants cannot be retried on counts for which they were acquitted. But on remand, Bravo-Fernandez and Martinez-Maldonado moved for judgments of acquittal on the vacated counts of conviction—the Section 666 bribery charges—invoking the issue-preclusion component of the Double Jeopardy Clause. They argued that they could not be retried on the bribery charges because the jury necessarily determined that they were not guilty of violating Section 666 when it acquitted them of conspiring to violate Section 666 and of traveling in interstate commerce to further violations of Section 666, given that the same issue of fact—the offer and acceptance of a bribe within the meaning of Section 666—was the basis for all three statutory offenses.

The district court disagreed, as did the First Circuit. In an opinion by Justice Ruth Bader Ginsburg affirming the First Circuit, the Court in *Bravo-Fernandez* held that issue preclusion does not apply where the mixed verdict does not reveal what the jury necessarily decided. Applying a strict textual read of the Double Jeopardy Clause, the Court reasoned that because inconsistency in the jury's verdicts could have been due to jury leniency and compromise, as opposed to factual determinations that the defendants were innocent, the defendants could not rely on issue-preclusion to bar retrial of the convicted counts.

In a separate concurrence, Justice Clarence Thomas argued that the original meaning of the Double Jeopardy Clause did not allow for an issue-preclusion prong at all, and urged the Court to reconsider the doctrine in an appropriate case.

Bravo-Fernandez is certainly a setback for defendants who faced multiple charges and seek to dismiss a

conviction on the basis of issue preclusion, although the full scope of its impact remains uncertain given the unique facts of this case. At a minimum, the decision should give prosecutors comfort that they can continue to bring overlapping charges arising out of the same basic facts, and a split verdict will not raise double jeopardy issues in this unique procedural scenario.

False Claims Act

State Farm Fire and Casualty Co. v. United States ex rel. Rigsby

In *State Farm*, the Court unanimously held that violating the False Claims Act requirement that certain complaints must be sealed for a limited time period does not mandate dismissal of a private party's complaint with prejudice.

The FCA's *qui tam* enforcement provisions—31 U.S.C. § 3729 *et seq*.—allow a private party known as a ''relator'' to bring an FCA action on behalf of the federal government against a defendant who ''knowingly presents . . . a false or fraudulent claim for payment or approval'' to the government. The Attorney General retains the authority to intervene in a relator's ongoing action or to bring an FCA lawsuit in the first instance. The seal provision was enacted to encourage more private enforcement lawsuits due in part to a lack of resources on the part of federal enforcement agencies and to allay the government's concern that a relator filing a civil complaint would alert defendants to a pending federal criminal investigation. The FCA requires that the complaint ''shall be filed in camera, shall remain under seal for at least 60 days, and shall not be served on the defendant until the court so orders.''

In 2006, former claims adjusters filed a *qui tam* complaint under seal alleging that State Farm instructed adjusters to misclassify wind damage from Hurricane Katrina as flood damage in order to shift petitioner's insurance liability to the government. Before the seal was lifted in part, respondents' then-attorney emailed a sealed evidentiary filing that disclosed the complaint's existence to journalists who then issued stories discussing the fraud allegations. The relators prevailed at trial, and on appeal, as the Fifth Circuit affirmed the district court's denial of State Farm's motion to dismiss based on the seal violation.

In an opinion by Justice Anthony M. Kennedy affirming the Fifth Circuit, the Court noted that the FCA does not explicitly require a dismissal remedy, and concluded on that basis that the FCA does not require dismissal of a complaint for violation of the seal provision. The Court also noted that such a remedy would undermine the very governmental interests that the seal provision is meant to protect.

Practitioners should take note that the Court advised that while not every seal violation mandates dismissal, nonetheless sanction remains a possible form of relief, as do other remedial tools short of dismissal, to punish and deter violations of seal provisions and other court orders.

Federal Criminal Procedure

Manrique v. United States

In *Manrique*, the Court held that where the initial judgment of conviction imposes certain aspects of a criminal sentence, such as imprisonment, but an amended judgment imposes restitution, a defendant appealing the restitution amount must file a notice of appeal following entry of the amended judgment—not merely following the initial judgment of conviction.

Under 18 U.S.C. § 3742 and Federal Rules of Appellate Procedure 3 and 4, a party must file a notice of appeal after the district court has decided the issue sought to be appealed. Applying a strict textual read to these procedural requirements, the Court held in a 6-2 decision authored by Justice Thomas that because the defendant's notice of appeal preceded the judgment imposing the actual restitution amount he sought to appeal, he failed to properly appeal under the applicable statute.

In dissent, Justice Ginsburg noted that the district court did not fulfill its obligation to notify Manrique of his right to appeal, and the district court clerk in this case transmitted the amended judgment directly to the Eleventh Circuit, which filed the amended judgment together on the docket with the conviction and sentence already pending appeal. Because even the court personnel presumed that the deferred restitution award was part of the appeal, Justice Ginsburg considered the clerk's transmission an adequate substitute for a second notice of appeal.

While this conviction involved possession of child pornography, it applies broadly to all criminal convictions in which aspects of the sentence are delayed. In white collar cases particularly, where restitution often is deferred and imposed following an initial judgment of conviction and sentence, practitioners must be mindful of the procedural requirements for an appropriate appeal.

U.S. Sentencing Guidelines

Beckles v. United States

In *Beckles*, the Court unanimously held that the Federal Sentencing Guidelines are not subject to vagueness challenges under the due process clause. Travis Beckles was convicted of possession of a firearm by a convicted felon and was given an enhanced sentence as a ''career offender'' under Section 4B1.1(a) of the guidelines because his offense qualified as a ''crime of violence'' under Section 4B1.2(a)'s residual clause, which defines a ''crime of violence'' as an offense that ''involves conduct that presents a serious potential risk of physical injury to another.''

In an opinion by Justice Thomas affirming the Eleventh Circuit, the Court held that as a result of the discretionary nature of the guidelines post-*Booker*, due process does not require that the guidelines provide notice of a specific sentence; rather, due process requires only that the defendant be on notice of the applicable statutory range which establishes the permissible bounds of the court's sentencing discretion.

Three justices authored separate concurring opinions. Justice Kennedy noted that it is possible that a future case might involve a sentence that is so arbitrary as to raise vagueness concerns and that the Court should not close the door altogether to Constitutional limitations based on vagueness. Justice Ginsburg noted that the official commentary to the guidelines allowed the case to be decided on narrower grounds so a broader ruling should be deferred to a future case. Justice Sotomayor agreed with Justice Ginsburg's conclusion and

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wrote separately to note that because the guidelines play a central role at sentencing, they should be subject to vagueness challenges under the due process clause.

October 2017 Term Cases

The Supreme Court has granted certiorari in a number of criminal and civil enforcement-related cases that will be argued in the October 2017 term.

Marinello v. United States

The Supreme Court recently granted certiorari in *Marinello*, which raises the question whether a conviction under 26 U.S.C. § 7212(a) for corruptly endeavoring to obstruct or impede the due administration of the tax laws requires proof that the defendant acted with knowledge of a pending Internal Revenue Service action. The Second Circuit affirmed, but Judge Dennis Jacobs wrote in dissent that Section 7212(a) should be read more narrowly because ''at some point, prosecutors must encounter boundaries to discretion.'' In recent years the Supreme Court has narrowly construed certain criminal statutes and reversed some convictions on the ground that the prosecutors have interpreted the language, and the scope of the criminal offense, too broadly—most recently in overturning the bribery conviction of former Virginia Gov. Robert McDonnell (R). *Marinello* could provide the Court with an opportunity for a similar ruling.

Digital Realty Trust Inc. v. Somers

Here the Court will consider whether Dodd-Frank's whistleblower protections for disclosures that are ''are required or protected under the Sarbanes-Oxley Act,'' apply only to individuals who disclose to the SEC, or extend to individuals who make disclosures only within a corporate entity. *See* 15 U.S.C. § 78u-6. The Ninth and Second Circuits have taken the broader view, while the Fifth Circuit has held that unless an employee reported to the SEC, he or she falls outside Dodd-Frank's protections.

Class v. United States

This case raises the question whether a guilty plea waives a defendant's right to challenge the constitutionality of the statute of conviction. Circuits are split on this issue:

- the First, Tenth, and D.C. Circuits hold that a guilty plea does operate as a waiver;
- the Third, Fifth, Sixth, Ninth, and Eleventh Circuits hold that post-plea challenges to the constitutionality of the statute of conviction may be made; and
- the Fourth, Seventh, and Eighth Circuits allow such challenges, but only when the challenge is to the statute on its face, not as applied.

City of Hays, Kansas v. Vogt

Here, the Court will consider whether a criminal defendant's Fifth Amendment rights have been violated where the prosecution uses compelled statements at a probable cause hearing but not at a criminal trial. Courts are split on this issue—the Third, Fourth, Sixth, and Eighth Circuits have held that the Fifth Amendment's protections against self-incrimination only attach at trial, while the Second, Seventh, Ninth, and Tenth Circuits have held that such protections also attach during certain pre-trial proceedings.

Other Potential Cases

Other circuit splits on the horizon that may ultimately be addressed by the Court include a split between the Tenth and D.C. Circuits concerning whether the process for appointing the SEC's administrative law judges (ALJs) violates the Constitution's Appointments Clause. The Tenth Circuit held in *Bandimere v. SEC*, 844 F.3d 1168 (10th Cir. 2016), that the current appointment process—in which ALJ's are not appointed by the President, a federal judge, or the agency head—violates the Constitution. The D.C. Circuit held in *Lucia v. SEC*, 832 F.3d 277 (D.C. Cir. 2016), that the current appointment process meets Constitutional standards, because SEC ALJs are not ''inferior officers'' subject to Appointments Clause restrictions. Lucia's cert petition remains pending, but given the importance of this issue and the Circuit split developing, the Court is likely to address this issue in the relatively near future. The issue has broad implications with respect to the manner in which the SEC and other agencies, including the FDIC, execute their enforcement authority. As Judges Carlos F. Lucero and Nancy L. Moritz noted in their dissent from the Tenth Circuit's denial of rehearing en banc, ''[t]here are currently over 1,500 ALJs working in at least 28 different federal agencies, presiding over hundreds of thousands of agency adjudications each year.''

Finally, the Court may address whether an email service provider that stores electronic materials abroad must comply with a warrant issued under 18 U.S.C. § 2703 seeking disclosure of those materials. In *United States v. Microsoft*, a warrant was issued for information for a particular user's account. Microsoft stored that data on a server in Ireland. Microsoft moved to quash the subpoena as an impermissible extraterritorial application of Section 2703. The Second Circuit initially sided with Microsoft, and on the government's petition for rehearing, split 4-4 (with three judges recused) and therefore denied the government's request. In its petition for certiorari, the government argued that review is warranted due in part to the risks to public safety and national security posed by the decision, which the government claims impedes its ability to investigate and prosecute crimes. Microsoft has argued that the Second Circuit appropriately applied the presumption against extraterritoriality and that such information should be obtained through a mutual legal assistance treaty and appropriate cross-border channels. Microsoft further argued that the Court should await Congress' action on this issue, given that amendments to the applicable Stored Communications Act (SCA) are currently under consideration. The Second Circuit is the only appellate court to have addressed these issues to date, and other providers are litigating numerous cases—currently pending before courts in at least four circuits—addressing the extraterritorial reach of the SCA. It remains to be seen whether the Court will await further development of the law in this area, or whether it will take up this high stakes, multi-faceted issue in the October 2017 term.

Update: The Supreme Court granted certiorari in the *Microsoft* case.