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White Collar Roundup - January 2017

Hacking Law Firms to Obtain Inside Information

Preet Bharara, the U.S. attorney for the Southern District of New York, announced the indictment of three Chinese defendants for hacking law firms. The defendants obtained inside information, which they "exfiltrated from the networks and servers of multiple prominent U.S.-based international law firms with offices in New York." According to Bharara, "[t]he defendants targeted at least seven law firms as well as other entities in an effort to unlawfully obtain valuable confidential and proprietary information," which they then used to make securities trades ahead of planned, but secret, mergers. The defendants obtained access to the firms by "using the unlawfully obtained credentials of a [firm] employee." They then "caused malware to be installed" on the firm's Web server, which contained e-mails of firm employees and partners. In several instances, the firm's partners were privy to the confidential potential mergers. The defendants then placed securities trades ahead of those mergers and reaped profits upon their consummation. Through their scheme, the defendants are alleged to have enriched themselves by millions of dollars. For a copy of the indictment, click here.

Second Circuit Rebukes the Fraud Guidelines

The appeal in *United States v. Algahaim* before the U.S. Court of Appeals for the Second Circuit appeared destined to end as most appeals do, with an affirmance. But the court chose instead to take a *sua sponte* swipe at the fraud guidelines and to remand for reconsideration of the admittedly non-erroneous sentence. The case involved a prosecution for stealing money from the federal Supplemental Nutrition Assistance Program (SNAP) by fraudulently exchanging SNAP payments for cash, which is prohibited by law. On appeal, the appellants, Ahmed Algahaim and Mofaddal Murshed, contended the jury charge was improper (both), claimed the evidence was insufficient to convict (Murshed), argued the district court improperly rejected a reduction in the guidelines because of a minimal role (Algahaim) and professed not to have been shown the presentence investigation report as required (Murshed). As is typical, the appeals court dispatched these arguments swiftly. But then the court began an assault on the fraud guidelines. The court first noted that the base offense level for each defendant was six and that because of the loss amount, 16 levels were added for Algahaim and 18 levels were added for Murshed, which was a threefold increase. The court noted that the U.S. Sentencing Commission had the authority to use "loss amount as the predominant determination of the adjusted offense level for monetary offenses." But it compared that choice to "other sentencing systems" and deemed its "unusualness" a "circumstance that a sentencing court is entitled to consider." As it said, "Where the Commission has assigned a rather low base offense level to a crime and then increased it significantly by a loss enhancement, that combination of circumstances entitles a sentencing judge to consider a non-Guidelines sentence." Because the district court in this case did not do so, the Second Circuit remanded for reconsideration, while noting that it was not ruling that the sentences "were in error." So while the sentences were legal and free of error, the court vacated and remanded anyway because it (apparently) strongly disagreed with the fraud guidelines.

Supreme Court's White Collar December

The Supreme Court issued two unanimous white-collar opinions in December. First, in *Salman v. United States*, the Court clarified what prosecutors in insider-trading cases must prove to a jury. In doing so, the Court rejected the more onerous standard previously endorsed by the Second Circuit. For analysis of the *Salman* opinion, click here. Second, in *Shaw v. United States*, the Supreme Court analyzed what it means to "defraud a financial institution," which is criminalized in the bank fraud statute. In *Shaw*, the defendant had been convicted of bank fraud after he defrauded a bank customer of funds held in

a bank account. Shaw argued he did not commit bank fraud because he had no intention to cause and did not cause the bank financial harm. In a sweeping rebuke, the Court explained that "the statute, while insisting upon 'a scheme to defraud,' demands neither a showing of ultimate financial loss nor a showing of intent to cause financial loss." The wrong criminalized by the statute is the victim's losing the chance to bargain based on accurate facts. This reasoning, which would likely apply as well to the mail fraud and wire fraud statutes and appears to be the first such proclamation from the Supreme Court, indicates that to be convicted of a federal fraud offense, no financial harm must be intended or caused by the purported fraudster. For analysis of the *Shaw* opinion, click here.

Possible Lifting of the Veil on the Secret "Blue Book"

The U.S. Court of Appeals for the D.C. Circuit issued an amended order in *National Association of Criminal Defense Lawyers v. Executive Office for United States Attorneys*. As we reported here and wrote more about here, the litigation revolves around the NACDL's efforts to obtain copies of the Department of Justice criminal-litigation manual, known as the "Blue Book." In July, the D.C. Circuit affirmed the district court's ruling to protect the Blue Book from disclosure, holding it was protected by the work-product doctrine. In response, the NACDL filed a motion for panel rehearing. The court denied that petition but ordered that its initial opinion be amended, directing the district court to "assess whether the Blue Book contains non-exempt statement of policy that are reasonably segregable [from] the protected attorney work product and therefore should be disclosed." Whether the NACDL will get to see any of the Blue Book after remand remains to be seen, but their rehearing petition appears to have given renewed—albeit narrow—hope in a lawsuit that looked dead in July.

SEC Administrative Action Cannot Be Halted in District Court

The Fourth Circuit in *Bennett v. SEC* joined the Second, Seventh, Eleventh and D.C. Circuits in holding that a defendant's challenge to the constitutionality of an SEC enforcement proceeding is premature. In the case, Dawn Bennett became the subject of an SEC administrative enforcement proceeding for violations of the Exchange Act. Bennett filed an action in U.S. District Court to enjoin the action, alleging that the administrative proceeding was unconstitutional. She alleged that the SEC's administrative enforcement proceedings violate Article II of the U.S. Constitution, which provides that the "executive Power shall be vested in a President of the United States," U.S. Const. art. II, § 1, cl. 1, and that "the Congress may by Law vest the Appointment of such inferior Officers, as they think proper . . . in the Heads of Departments," *id.* § 2, cl. 2. She claimed that "(1) ALJs count as 'inferior Officers' and that the SEC's Commissioners—collectively a 'Head' of a 'Department'—failed to appoint them, and (2) those ALJs enjoy at least two levels of protection against removal, which impedes presidential supervision over their exercise of 'executive Power' and thereby contravenes the separation of powers." The district court dismissed the case, and the Fourth Circuit agreed, reasoning, among other things, that the Exchange Act authorized appeals from agency determinations, which renders that the exclusive method of obtaining jurisdiction in federal courts. As a result, Bennett must proceed to litigate the administrative action and, should she lose, appeal to the appropriate court of appeals as set forth in the Exchange Act.

Off-the-Cuff and Regrettable

At a Federalist Society panel, Assistant Attorney General Leslie Caldwell made some off-the-cuff remarks about the fact that the "quality of the lawyers" varies between U.S. attorney's offices. She recognized "there are cases that get filed that shouldn't be filed. There are districts where the oversight is not what it should be. The experience level is not what it should be." She also noted that prosecutors in the field—as opposed to those at Main Justice—are less likely to make their decisions in line with the guidance of the *U.S. Attorneys Manual* and that her office has intervened on occasions when local offices were poised to make poor decisions. As an example, she recounted a time in which a U.S. attorney sought to indict two partners at a major law firm for seeking additional time to respond to a subpoena, which is a run-of-the-mill request in white-collar cases. As one might imagine, some prosecutors took umbrage at her remarks. That blowback prompted Caldwell to apologize for her comments in a widely circulated letter. Caldwell expressed genuine contrition, saying, "I deeply regret my remarks and the genuine hurt they caused. As a federal prosecutor for 19 years . . . I know better."

Before the Above-mentioned Storm, a Few Words About Cybercrime

The day before kicking off the aforementioned kerfuffle, Caldwell spoke at the Center for Strategic and International Studies about the DOJ's efforts to fight cybercrime. At the start, she noted that "some of the most significant hurdles" that the DOJ encounters in prosecuting crime today "relate to technology and the Internet." She explained that while the Internet "has had tremendous benefits for our economy, our ability to connect with others, and the convenience, efficiency, and security of our everyday lives," it has also allowed "criminals to more easily victimize Americans, including from afar, while concealing their identities and enabling destruction of evidence." Caldwell focused on four challenges facing the DOJ: (1) "the growth of sophisticated, global cyber threats"; (2) "dangerous loopholes in our legal authorities"; (3) "the widespread use of warrant-proof encryption"; and (4) "inefficient cross-border access to electronic devices." Caldwell catalogued many of the DOJ's successes, while highlighting the challenges faced and arguing for changes in laws and regulations, such as the venue-provision amendments to Federal Rule of Criminal Procedure 41, which will allow law enforcement to more easily obtain search warrants for electronic devices.

The Dangers of Secretly Auto-forwarding Emails

The Seventh Circuit in *Epstein v. Epstein* had the opportunity to decide whether an aggrieved wife's setting up an auto-forward of her husband's emails violated portions of the Wiretapping and Electronic Surveillance Act. The case arose as follow-on litigation to the acrimonious divorce between Paula and Barry Epstein. In that matter, Paula accused Barry of serial infidelity, prompting Barry to ask for supporting evidence in discovery. Paula obliged, sending scores of emails between Barry and several other women. Upon receipt, Barry alleged in federal court that "Paula violated the Wiretap Act by surreptitiously placing an auto-forwarding 'rule' on his email accounts that automatically forwarded the messages on his email client to her." The district court dismissed the complaint upon Paula's Rule 12(b)(6) motion, which claimed that the Wiretap Act requires contemporaneous interceptions, which it found were not present here. Barry appealed. Under the Wiretap Act, anyone who "intentionally intercepts [or] endeavors to intercept . . . any wire, oral, or electronic communication" or who uses any "unlawfully intercepted electronic communication" is guilty of a federal crime. The Seventh Circuit noted, "Several circuits have held that the Wiretap Act covers only contemporaneous interceptions—understood as the act of acquiring an electronic communication in transit—rather than the acquisition of stored electronic communications." It reasoned, however, that it need not resolve that issue because Barry had alleged Paula intercepted the emails in transit. The district court's assumption that the emails were copied after they were transmitted was premature; to the contrary, because the court dismissed Barry's case on the pleadings, the district court did "not know how Paula's auto-forwarding rule worked." As a result, the Circuit reinstated the lawsuit.

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