

# Fighting On Two Fronts: Parallel Proceedings And Challenges At The Intersection Of Criminal And Civil Law

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Perhaps there was a time when the term "parallel proceedings" was not part of the vocabulary of in-house counsel and private practitioners. If that were ever true, it is certainly not the case today. Parallel proceedings, and the challenges they give rise to, in terms of legal issues and strategic choices, have become commonplace.

## Defining The Terms

As a general rule, parallel proceedings is a term that refers to two different circumstances. The first involves two actions, one civil and one criminal, both brought by the government, either concurrently or successively, in which the allegations of unlawful conduct arise out of the same set of facts. The second involves two actions, again arising out of the same facts or transactions, and again concurrent or successive, one of which is brought by the government as a criminal prosecution or enforcement action, while the other is brought as a civil action by a private plaintiff.

## Double Trouble: When The Government Invokes Both The Criminal And Civil Process

Does the government have the power to conduct parallel civil and criminal proceedings, or should it be required to make a choice as to how to respond to perceived unlawful conduct? The Supreme Court supplied the answer to this question in *United States v. Kordel*, 379 U.S. 1 (1970), in which it stated that "[I]t would stultify enforcement of federal law to require a government agency...invariably to choose either to forgo recommendation of a criminal prosecution once it seeks civil relief, or to defer civil proceedings pending the ultimate outcome of a criminal trial."

The government has taken steps as an institutional matter to encourage the double-barreled approach. In 1997, the Justice Department issued a memorandum to all federal attorneys instructing them to increase the efficiency and reach of the government's enforcement efforts by developing "greater cooperation, communication and teamwork between the criminal and civil prosecutors who are often conducting parallel investigations of the same offenders and matters."<sup>1</sup>

However, in three recent decisions, courts have reacted negatively to the government's invocation of both civil and criminal processes in parallel proceedings.

## SEC v. Saad: Defendants Facing Parallel Proceedings Are Entitled To Timely Discovery In The Civil Case In Securities Exchange Commission v.

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*Saad*, 229 F.R.D. 90 (S.D.N.Y. 2005), Judge Jed S. Rakoff of the Southern District of New York denied a government application for a stay of discovery in an SEC enforcement action which had been filed in tandem with a parallel criminal case. In doing so, Judge Rakoff pointed out that the government could not always use the judicial process exclusively to its own advantage. In *Saad*, the government supported the stay application on the ground that the civil process would permit the defendants to gain a "special advantage" because of the broader discovery of the government's case it would be entitled to under Rule 26 of the Federal Rules of Civil Procedure. Judge Rakoff held that the government's position was difficult to credit where "the U.S. Attorney's Office, having closely coordinated with the SEC in bringing simultaneous civil and criminal actions against some hapless defendant, should then wish to be relieved of the consequences that will flow if the two actions proceed simultaneously."<sup>2</sup>



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## SEC v. HealthSouth: SEC's Use Of Evidence Derived From Criminal Investigation For Civil Application Can Result In Unfairness

In connection with an application to freeze the assets of the then unindicted Richard Scrushy, Chairman and CEO of HealthSouth Corporation, the SEC supported its application by introducing (1) testimony of an FBI agent involved in the criminal investigation that later led to the indictment against Scrushy, (2) tape recorded conversations between Scrushy and a former HealthSouth officer who had been outfitted with a recording device by the FBI and the U.S. Attorney's Office and instructed by them to obtain incriminating statements from Scrushy; and (3) guilty plea colloquies of former HealthSouth officers who had negotiated plea agreements with the U.S. Attorney's Office but who were not subject to cross-examination by Scrushy's counsel due to their assertion of their privilege against self-incrimination.

The district court denied the asset freeze application on the ground that the SEC had used evidence at the hearing from the criminal investigation as support for an application civil in nature, the guilty plea colloquies could not be considered because of the lack of cross-examination, and the government had improperly refused to provide Scrushy with a copy of the tape recording – a refusal it sought to justify on the ground that it lacked authority to do so because the tape recording was FBI property.<sup>3</sup>

## United States v. Stringer: Deliberate Use Of Civil Process With The Intention To Use Its Fruits To Bring An Indictment Can Violate Due Process

Earlier this year, a district judge in Oregon dismissed a federal indictment and suppressed evidence gathered by the SEC on the ground that federal prosecutors had used the SEC to obtain evidence from the subjects of the investigation

while concealing the existence of the criminal investigation. The court found fault because the U.S. Attorney's Office had directed the type of evidence it wanted the SEC to gather while the SEC sidestepped the defendants' efforts to learn whether, while cooperating with the SEC, they were targets of a criminal investigation.<sup>4</sup> In February 2006, the U.S. Attorney's Office appealed the district court's decision, and the SEC has filed an amicus brief. Oral argument has yet to be scheduled.

It would be premature to conclude that the *Saad*, *Scrushy*, and *Stringer* decisions will undermine the government's otherwise valid ability to conduct parallel civil and criminal proceedings. However, these cases may be the "canary in the coal mine" as far as the government is concerned. In other words, these cases may be an early warning signal to the government that courts will not tolerate government conduct in the context of parallel proceedings which appears to be unduly manipulative or seeks unfair tactical advantages.

## Private Civil Actions And Criminal Prosecutions: Parallel Proceedings That Create Special Dangers

The other common form of parallel proceedings consists of a simultaneous or successive criminal investigation or prosecution and a related private action for damages. The following hypothetical may be instructive.

Assume your company has received a grand jury subpoena calling for the production of documents related to certain aspects of the company's business. Further assume that the prosecutor who issued the subpoena will not give any assurances about the scope of the investigation, its subjects, or likely targets. Grand jury subpoenas are then served calling for the testimony of various officers and employees. A civil complaint is then filed setting forth allegations that relate to the same aspects of the company's business that the grand jury is investigating. Document discovery requests and deposition notices in the civil case follow.

## Avoiding Self-Incrimination And The Adverse Inference: Applications For Stays And Protective Orders

While the company, which has no Fifth Amendment privilege, will produce its documents, the individuals may decline to testify before the grand jury if doing so risks self-incrimination. *Kastigar v. United States*, 406 U.S. 441 (1972). However, if they rely on the privilege in a civil deposition, they run the risk that a finder of fact, such as a judge or civil jury, may draw adverse inferences against them – and in some circumstances attribute those inferences to another party, including a corporation – from the refusal to answer deposition questions. *Baxter v. Palmigiano*, 425 U.S. 306 (1976).

To bypass providing evidence in the civil case while also avoiding the adverse inferences, an application for a stay of the civil proceeding may be made during the pendency of the criminal case. If granted, the looming civil depositions can be postponed and the criminal investigation can become the sole focus. In response to such an application, the civil plaintiff typically argues that the right to proceed with its case should not be held hostage to the

pace of the criminal case. The government, for its part, aims to take advantage of the dilemma confronting the subject of the investigation, hoping that the extreme pressure exerted on those it is investigating will often speed up the resolution of the criminal case.

Courts have identified a number of factors to be considered in deciding how to rule on the stay requests, including the interest of the civil plaintiff in proceeding without undue delay, the burden on the defendant in the civil case who is also contending with the criminal process, the interest of the public in the pending criminal and civil matters, and the court's own concern in the sound management of its docket. If the criminal investigation is at an early stage, the case for what may seem to be an indefinite stay of the civil action is weak. On the other hand, if the criminal investigation is coming to a conclusion, or an indictment has actually been returned, the case for a temporary stay of relatively short and more certain duration is stronger. *See e.g.*, Judge Pollack's remarks at a 1989 judicial conference, entitled "Parallel Civil and Criminal Proceedings," reprinted at 129 F.R.D. 201.

## Protective Orders

A company or individual can also seek a protective order, pursuant to Rule 26 of the Federal Rules of Civil Procedure, precluding the disclosure of civil discovery to criminal investigators and the grand jury. If a protective order is entered, then the civil discovery, including deposition testimony, can go forward, free of the risk that such testimony will be utilized in the criminal case. The courts are divided on such applications. Compare *Minpeco S.A. v. Conticommodity Services, Inc.*, 832 F.2d 739 (2d Cir. 1987) (protective order appropriate in absence of strong showing to the contrary) with *In re Grand Jury Subpoena*, 836 F.2d 1468 (4th Cir.), *cert denied*, 487 U.S. 1240 (1988); *In re Grand Jury Proceedings*, 995 F.2d 1013 (11th Cir. 1993); *In re Grand Jury Subpoena*, 62 F.3d 1222 (9th Cir. 1995) (protective orders to keep civil discovery from grand jury denied).

## Conclusion: No Neat And Tidy Solution

Despite the possibility of heightened judicial scrutiny and intervention, as illustrated by cases such as *Saad*, *Scrushy*, and *Stringer*, it would be overly optimistic to conclude that coordinated civil and criminal law enforcement efforts by the government, giving rise to consecutive or simultaneous government proceedings, and parallel criminal cases and parallel private civil actions, are on the wane. A safer prediction would be that these issues will continue along the same, or an accelerated, trend line, due to the current environment of highly active government responses to the perception of corporate wrongdoing. Consequently, those who advise, counsel, and represent corporate and individual clients will be compelled to meet the continuing challenges presented by such parallel proceedings.

<sup>1</sup> Memorandum from the Attorney General to Federal Attorneys (July 28, 1997).

<sup>2</sup> 229 F.R.D. at 92.

<sup>3</sup> SEC v. HealthSouth Corp., 261 F. Supp.2d (N.D. Ala. May 7, 2003).

<sup>4</sup> United States v. Stringer, 408 F. Supp. 2d 1083 (D. Ore. 2006).

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