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By: David E. Frank May 15, 2014

White-collar lawyers say gone are the days when a civil suit brought by the Securities and Exchange Commission is stayed simply because the U.S. attorney is prosecuting a parallel criminal case.

The latest example illustrating the new reality: *Securities and Exchange Commission v. K2 Unlimited, Inc., et al.* (Lawyers Weekly No. 02-241-14). U.S. District Court Judge Mark L. Wolf denied a defense request to suspend an SEC suit over the fraudulent sale of fictitious investment instruments against defendant Diane Glatfelter while U.S. Attorney Carmen M. Ortiz in Boston prosecuted Glatfelter for wire fraud.

When the SEC announced its intention to depose Glatfelter on May 1, she unsuccessfully moved for a stay until the end of her criminal case, scheduled for trial in September before U.S. District Court Judge Douglas P. Woodlock.

"It used to be that these cases were stayed automatically pending the resolution of the criminal matter for a number of reasons, not the least of which was conservation of court resources," said Luke T. Cadigan of K&L Gates in Boston. "However, more and more judges are making the decision that if the SEC is going to file the case when it does, they're going to make it go forward with the understanding that justice needs to be served and these cases need to proceed."

Cadigan, former assistant director in the enforcement division of the SEC's Boston office, said that means Glatfelter and defendants like her must decide whether to be deposed or exercise their Fifth Amendment right to remain silent.

Complicating the matter is that defendants who do not testify risk being on the receiving end of a damaging adverse instruction from the court, allowing jurors to consider their silence at trial.

"As a legal matter, all it does is allow the fact-finder to take into account the refusal to answer questions at the deposition amongst other evidence, and can't provide the sole basis for a determination of liability," Cadigan said. "But as a practical matter, it can have a dramatic impact on the way the jury views the defendant, because unfortunately there's an assumption that if you take the Fifth, you're liable or guilty of the conduct you're being questioned about."

Ian D. Roffman, a partner in Nutter, McClennen & Fish's securities enforcement and litigation practice group, said that, until recently, it was not only defendants requesting stays.

The SEC routinely asked the court to put its case on hold in favor of a criminal action, he said. But Roffman, who served as senior trial counsel for the SEC in Boston from 2001 to 2007, said those days are over as well.

"It rarely happens — at least in this district — anymore because judges simply won't allow it," he said. "It was the SEC's view that it would let the U.S. Attorney's Office prosecute the criminal case, and depending on how it was resolved, it would often have a big impact on how its own case was disposed."

The SEC frequently filed jointly with federal prosecutors to more easily obtain an asset freeze or other relief. At that point, the parties would typically agree to let the criminal matter drive the proceedings, Roffman said.

"But in the past few years, we've seen a number of instances in which judges said to the SEC, 'If you're going to bring a case, you should expect to prosecute that case,'" he said. "You can't simply file a case with the expectation that you can sit on your hands and not follow through on an action that you started."

Slow down

Michael P. DeMarco of Wellesley, counsel to Glatfelter in the civil case before Wolf, recently moved for the stay over the SEC's objections.

DeMarco made his request after learning that the SEC, which filed suit in 2011, planned to depose his client on May

1. Wolf denied the motion, in part, because he found the allegations in the criminal and civil matters were sufficiently unrelated.

The criminal indictment alleged Glatfelter committed wire fraud by accepting payment from a single victim in exchange for a false promise to provide a loan.

The civil suit involved a different, broader scheme, the judge said.

"Most of the factual allegations and all of the claims for relief [by the SEC] focus on the defendants' solicitation of investments in fraudulent securities," Wolf wrote. "The allegations at the heart of the criminal indictment are, therefore, not encompassed by the claims for relief in the civil complaint."

DeMarco did not return calls for comment. Deena R. Bernstein of the SEC declined to discuss the case.

No need for a head start

Despite Wolf's conclusion that the SEC and criminal matters were sufficiently unrelated, Boston lawyer Martin G. Weinberg said he could not envision a circumstance in which he would instruct a client to be deposed with an indictment pending.

"Even with a client who's truthful and could fully testify, it would be devastating in a parallel prosecution to essentially provide the U.S. Attorney's Office a detailed script of what his testimony will be by sitting down for a deposition with the SEC," Weinberg said.

The veteran criminal defense lawyer added that most people are more concerned about their liberty over licensing and money, and few have the resources and energy to defend two federal matters at the same time.

"Just like the government doesn't allow a criminal defense lawyer to depose its witnesses, why give the government a six-month head start at impeachment by allowing the client to be deposed?" Weinberg asked. "I think it's simply inexorable that you are diminishing his ability to successfully withstand cross-examination by providing a 200- or 300-page transcript of your client's story ahead of time."

While Weinberg agreed that the adverse inference jury instruction can be highly prejudicial, he said the benefits of allowing dual investigations to proceed at the same time outweigh the negatives. The SEC action permits the defense to gather "enormous amounts" of discovery that would otherwise be unavailable in the criminal matter, he said.

"There is at least precedent to support the idea that, when there's parallel litigation, the U.S. Attorney's Office has an obligation to get, review and then provide any exculpatory evidence generated in the SEC case, so I welcome parallel litigation and hope that the government doesn't look to stay the civil case," he said. "An active civil case can generate important information that might not be immediately available because the U.S. attorney doesn't know of it absent some order that they review the SEC files."

Stephen F. Gordon of Boston said the 1st U.S. Circuit Court of Appeals has identified a number of factors judges typically weigh when ruling on motions to stay:

the rights of the SEC to proceed expeditiously with the civil litigation; the hardship dual prosecutions would create on a defendant; judicial economy; and interest to the public and third parties.

Gordon argued a 1st Circuit case, *Microfinancial, Inc. v. Premier Holidays Int'l*, which was cited by Wolf. The decision required judges to also take into account the procedural status of the criminal and civil cases, as well as the good faith of the party seeking the stay.

"Everyone likes when a high appellate court like a circuit court gives you a series of steps to follow, which is what happened in the *Microfinancial* case," Gordon said. "What the 1st Circuit has done is lay out a series of questions that need to be answered whenever a request to slow down a civil suit is brought. But at the end of the day, these really important issues boil down to matters of judicial discretion."

The seven-page ruling in *Securities and Exchange Commission v. K2 Unlimited, Inc., et al.* can be found by clicking here.

Issue: MAY 19 2014 ISSUE