CFO

In today's high-stakes legal environment, top white-collar attorneys are ready to defend the CFO.

By Kate O'Sullivan

The Best Defense

Last year, former McKesson Corp. CFO Richard Hawkins faced criminal charges after a $20 million accounting error was discovered at HBO & Co., a subsidiary McKesson had acquired in 1999. Together, the charges, including securities fraud and conspiracy, carried a maximum sentence of 25 years in prison. With executives from Tyco, WorldCom, and HealthSouth also on trial, and with public outrage at corporate scandals mounting, Hawkins decided to take a gamble: he waived his right to a jury trial.

> THE SURGE IN FINANCE-RELATED CASES HAS BEEN ACCOMPANIED BY INCREASED PUBLIC INTEREST—AND ANGER. "SINCE ENRON, THERE'S BEEN A HUGE AMOUNT OF HATRED DIRECTED AT CEOs AND CFOs," SAYS KEKER.
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> **JOHN KEKER,** KEKER & VAN NEST LLP

"We didn't have a lot of comfort that a jury would take the time to wade through the accounting rules—particularly in this climate, with so many other executives going to trial at the same time," explains Walter F. Brown Jr., a partner at Orrick, Herrington & Sutcliffe LLP in San Francisco and a co-leader of Hawkins's defense team. The gamble paid off. The defense convinced the judge that the former CFO had made accounting judgments in good faith, after consulting with outside auditors. Hawkins was found not guilty on all counts, one of the few recent victories for a CFO on trial.

The verdict solidified Brown's status as a member of a legal elite: the 50 or so white-collar defense attorneys who are regularly tapped to represent top executives of America's largest companies. They include such stars as John Keker of Keker & Van Nest LLP in San Francisco, attorney for former Enron CFO Andrew Fastow; Reid Weingarten of Steptoe & Johnson LLP in Washington, D.C., who defended former WorldCom CEO Bernard Ebbers and is currently representing former Enron chief accountant Richard Causey; and Charles Stillman of Stillman & Friedman PC in New York, who defended former Tyco finance chief Mark Swartz.

This cream of the white-collar defense bar has been busy the past few years, as regulators and prosecutors have stepped up their pursuit of corporate wrongdoers. Civil and criminal investigations have focused on aggressive financial and accounting tactics, making finance executives inevitable targets of litigation. Companies are quick to distance themselves from accused CFOs, who are often pressured to cooperate with prosecutors or face the possibility of stiff penalties and prison sentences.

In this high-pressure, high-stakes environment, a finance executive needs the best legal help he or she can find—and afford.

The Howling Mob

Many top white-collar defense attorneys got their start on the other side of the aisle, as prosecutors. Many know one another, personally or by reputation; some worked in the same U.S. Attorney's office. As a result, it's clubby at the top, with attorneys regularly referring business to one another when schedules fill up or conflicts arise.

Those schedules have been filling rapidly with finance-related cases as the government has cracked down on corporate crime. For instance, Brown says 25 to 35 percent of his work involves finance executives, as defendants in civil or criminal investigations. Weingarten of Steptoe & Johnson says about half of his practice is devoted to defending finance executives, compared with 10 to 20 percent prior to 2001.

The surge in finance-related cases, often involving many millions of dollars of shareholder value, has been accompanied by increased public interest—and anger. "We're living in this environment where it's like you're defending a nobleman in the French Revolution, and the guillotine is outside and the mob is howling," says Weingarten. Keker agrees: "Since Enron, there's been a huge amount of hatred directed at CEOs and CFOs."

Accounting maneuvers that were once praised in the financial

Photograph: Robert Houser

press as earnings management are now attacked in the courtroom as fraud. "We're seeing cases of accounting improprieties that are being prosecuted criminally today that would not have been prosecuted that way 10 years ago," says David Schertler, a founding partner at Washington, D.C.-based Schertler & Onorato LLP. In 2002, Schertler defended WorldCom's former director of accounting, Buford Yates, against securities-fraud charges. Agreeing to cooperate with investigators, Yates pleaded guilty and received a prison sentence of one year and one day.

It could have been worse for Yates, as prosecutors are seeking tougher plea agreements and longer jail sentences for white-collar defendants. "Suddenly, all people want to do is put chief financial officers in prison," says Charles Stillman, who defended Tyco's Swartz against fraud and larceny charges. "That's the game du jour."

Cram Sessions

To have a shot at winning this game, defense attorneys have to digest complicated financial matters in a hurry. "Often these cases rise and fall on complex accounting issues and your ability to understand them," says Brown, who studied the fine points of revenue recognition and the accounting rules regarding reciprocal transfer, or rights of return, for the McKesson case. "There is no substitute for immersing yourself in the GAAP literature and mastering it." Brown has taken classes designed for lawyers who practice in finance-related areas, and says his firm has brought in representatives from the Big Four accounting firms to conduct seminars.

Few top attorneys have accounting or finance degrees, yet they must be able to parse the transactions at issue in a given case. "You have to know them backwards and forwards," says Dan Webb, a partner at Chicago's Winston & Strawn LLP who was named the country's best white-collar criminal lawyer in a poll of his peers (see "Cream of the Crop," this page). "Then you figure out the best and most straightforward explanation as to why it's not fraud."

Still, defense attorneys know there are limits to their financial expertise. That's why outside experts form a key part of any CFO defense, says Michael DeMarco, a partner at Kirkpatrick & Lockhart Nicholson Graham LLP in Boston. "I learned a long time ago that if you don't actually work in accounting every day, you've got to hire a competent consultant or forensic accountant to work with you," he says. Some attorneys will use a team of accountants to help them get an initial grasp of the issues in a case; and if a case goes to trial, they may call on other experts, often academics, to take the stand. (All of the Big Four firms have forensic-accounting divisions available for hire, and there are smaller boutiques that specialize in the field.)

But the greatest resource for a lawyer trying to master arcane accounting topics can be his client, say many top defenders. "A CFO, controller, or other finance person who's well educated and may have significant experience at a Big Four accounting firm can be a tremendous source of information," says Brown. "You should never underestimate what a client can bring to his own defense."

N. Richard Janis, a partner at the white-collar litigation boutique Janis, Schuelke & Wechsler in Washington, D.C., says David Myers, the former WorldCom controller whom he represented,

CREAM OF THE CROP

In a 2003 poll of white-collar criminal defense attorneys by newsletter *Corporate Crime Reporter,* the following attorneys were selected as those the respondents themselves would hire.


1. **Dan Webb;** Winston & Strawn; Chicago


2. **John Keker;** Keker & Van Nest; San Francisco


3. (tie) **Reid Weingarten;** Steptoe & Johnson; Washington, D.C.


3. (tie) **Brendan Sullivan Jr.;** Williams & Connolly; Washington, D.C.


4. **Robert Bennett;** Skadden, Arps, Slate, Meagher & Flom; Washington, D.C.


5. **Thomas Green;** Sidley Austin; Washington, D.C.


6. **Earl Silbert;** DLA Piper Rudnick Gray Cary; Washington, D.C.


7. **Daniel Reidy;** Jones Day; Chicago


8. **Robert Fiske Jr.;** Davis Polk & Wardwell; New York


9. (tie) **Theodore Wells Jr.;** Paul, Weiss, Rifkind, Wharton & Garrison; New York


9. (tie) **Plato Cacheris*;** Trout Cacheris; Washington, D.C.


10. **Robert Morvillo;** Morvillo, Abramowitz, Grand, Iason, & Silberberg; New York

*With Baker & McKenzie in 2003

Source: *Corporate Crime Reporter*

"THESE CASES RISE AND FALL ON COMPLEX ACCOUNTING ISSUES AND YOUR ABILITY TO UNDERSTAND THEM," SAYS BROWN. "THERE IS NO SUBSTITUTE FOR IMMERSING YOURSELF IN THE GAAP LITERATURE AND MASTERING IT."

WALTER BROWN, ORRICK, HERRINGTON & SUTCLIFFE LLP

helped him quickly grasp the critical accounting issues in that case. "These people are sophisticated, intelligent, and concerned, and they are going to help you get your hands around the facts as quickly as possible," says Janis. "Remember, the client has more than a rooting interest in the outcome."

Making the Case

If mastery of the numbers were all that mattered, CFOs would defend themselves. Defense strategies emerge from applying a legal perspective to accounting, says Paul Grand, a partner at Morvillo, Abramowitz, Grand, Iason & Silberberg PC in New York who defended Timothy Rigas, former CFO of cable operator Adelphia. Top attorneys not only devise trial strategy but often come up with the business rationale or accounting theory for the defense as well. Says Grand, "We're the ones who evaluate what sells in the courtroom."

The first goal is to avoid appearing in the courtroom at all. If a client engages an attorney early enough in the course of an investigation, and if the facts support him, the attorney can try to convince a prosecutor not to bring a suit. In a recent example, Jeffrey E. Stone, a partner at McDermott Will & Emery in Chicago, former head of the firm's white-collar practice and now head of the trial department, represented an insurance-company finance executive who was under investigation by New York State Attorney General Eliot Spitzer. "We lined up all the other cases where Spitzer had not prosecuted," recalls Stone. "We were able to argue that our facts were less egregious than in the other cases. He had to decline to prosecute my client in the interest of fairness and consistency." (Only a handful of people know the executive was close to being indicted.)

Inevitably, however, there will be cases in which charges are brought. And compared with other top company officials, the CFO is at a disadvantage in a fraud case: it's much harder for him to convince a jury that he didn't know what was happening with the company's finances. Such a "Sergeant Schultz defense," expected to be made by former Enron chairman and CEO Kenneth Lay, would have been very difficult for former CFO Fastow to have used credibly. Last December, just weeks before his trial was scheduled to begin, Lay publicly proclaimed his innocence, reiterated his position that "Enron was a strong, profitable, growing company even into the fourth quarter of 2001," and blamed Fastow for the company's collapse. (Jurors may not find this defense believable for Lay, either; Ebbers tried it without success.)

Nevertheless, in some cases, considering the intricacies of many frauds as well as the layers of management involved, CFOs may truly not know about all of a company's transactions. Lawyers often try to make that case. "There's a predilection to say, 'Oh, he was the chief financial officer; he knew everything,' but that's not necessarily true," says Grand. In the McKesson case, for example, Brown says Richard Hawkins testified at length about his responsibilities as the CFO of a *Fortune* 50 company before answering questions about the allegedly improper activities at the health-care services and information-technology business. "He talked about the far-reaching geography and functions he supervised, the reports he received on a regular basis, the reporting structure," recalls Brown. "The judge could understand at the end of the day that every issue might not come to his attention." This testimony created the foundation for the defense that Hawkins was unaware of the decision made by managers at a subsidiary to backdate a $20 million contract.

Sometimes, however, the client's involvement is all too clear. "In some cases, you're doing damage control," says Janis. "Before I began representing [WorldCom's Myers], he had basically acknowledged the accounting fraud to the internal investigators, the external auditors, and the board." Like Buford Yates, Myers pleaded guilty and received a jail sentence of a year and a day. "No lawyer likes to have a client go to prison," comments Janis. "But given the fact that he was in the middle of the fraudulent activity and that he had acknowledged it, it could have been a lot worse."

In such situations, cooperating with prosecutors may be the best strategy for finance executives. In the WorldCom case, for example, former finance chief Scott Sullivan pleaded guilty to securities fraud after arguing his innocence for two years. His cooperation enabled the government to indict Ebbers, and he became the government's star witness against his former boss. Sullivan, who estimated he spent some 400 hours working with prosecutors, likely received a double-digit reduction in his sentence due to his helpful and extensive testimony, says Stone (who was not involved in the case), despite the fact that Judge Barbara Jones called him the "architect" of the WorldCom fraud.

Similarly, the five former HealthSouth CFOs who pleaded guilty and testified against former CEO Richard Scrushy received relatively light sentences in part because of their cooperation, although Scrushy eventually won an acquittal. Meanwhile, Richard Causey, the former Enron chief accountant who recently pleaded guilty to a single count of securities fraud less than a month before his trial was scheduled to begin, now faces up to seven years in prison, with a possibility for a reduction to five years if the prosecutors determine that he has acted in good faith.

> STONE PERSUADED ELIOT SPITZER NOT TO INDICT HIS CLIENT, AN INSURANCE COMPANY EXECUTIVE. "WE WERE ABLE TO ARGUE THAT OUR FACTS WERE LESS EGREGIOUS" THAN IN OTHER CASES WHERE SPITZER HAD NOT PROSECUTED, SAYS STONE.
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> **JEFFREY E. STONE,** PARTNER AT McDERMOTT WILL & EMERY

For a defendant who had faced 36 counts of conspiracy, fraud, insider trading, lying to auditors, and money laundering, the deal looks quite a bit less risky than going to trial in Houston, Enron's hometown.

Ultimately, most cases turn on the definition of fraud. If a defense attorney cannot avoid charges and cannot argue that his client was not involved in the alleged improprieties, he turns to

the gray area: Did my client know that what he was doing was wrong?

"Accounting is not a black-and-white science," says Schertler. "If you're embezzling money, you know it's a crime. If you're dealing drugs, you know it's a crime. But what we've always focused on in accounting fraud is: Is this really a crime?" Adds Keker: "You want to show that matters of judgment are not matters of criminality. What's happened in the last few years is that people have used hindsight to label as criminal things that at the time were considered cutting-edge."

For example, in the 2004 "Nigerian barge" trial—regarding a 1999 agreement by Merrill Lynch to buy Enron's stake in three power-generating barges on the condition that Enron would buy them back at a price that would mean a profit for Merrill Lynch—Keker, who was not directly involved in the case, says executives at both companies had extensive discussions about whether the transaction was legal, decided it was, and proceeded. At trial, the court decided otherwise, and prison sentences for four former Merrill Lynch bankers and a former Enron vice president followed.

SOMETIMES IT'S BETTER TO SAY NOTHING AT ALL.

Taking the Stand

Should an executive on trial testify in his own defense? That is "perhaps the single most difficult and important decision in trial strategy," says Jeffrey E. Stone, a partner at McDermott Will & Emery. The results can vary widely, and can depend as much on the defendant's personality as on the facts of the case.

Juries often expect to hear accused executives present their side of the story, say defense attorneys. However, "if you put a client on the stand, the entire focus of the case will change immediately," says Dan Webb, a partner at Winston & Strawn in Chicago. Although the burden of proof rests with the prosecution, juries tend to forget that when a defendant testifies. **"Jurors are no longer focused on the government; they're focused on my client,"** says Webb. **"The entire case will rise and fall on whether they believe my client."**

The tactic has had mixed results for finance executives recently. On one hand, the testimony of former McKesson Corp. CFO Richard Hawkins about his role at the company formed a key part of the defense that led to his acquittal in a trial before a San Francisco judge. Former Tyco CFO Mark Swartz, however, was not as convincing on the stand. Swartz was convicted by a New York jury and is appealing his $8^{1}/_{3}$-to-25-year prison sentence.

—K.O'S.

When Things Go Wrong

Of course, even the best lawyers occasionally come up short in the courtroom. Strategies backfire, facts prove flimsy, outside influences play a decisive role. Weingarten says he is still "grieving" the outcome of the Ebbers trial, which he tried unsuccessfully to have moved to Mississippi, a location he believes would have been more sympathetic than the New York stage on which Tyco CEO Dennis Kozlowski and CFO Swartz were also convicted. A hometown location (Birmingham, Alabama) provided a tremendous advantage to Richard Scrushy, points out Weingarten. He had also hoped for success with a jury that was not Wall Street savvy, having won an acquittal for former Tyco general counsel Mark Belnick with a similar jury. "This one didn't work out so well," says Weingarten.

Countering government charges that Swartz had looted Tyco for his own gain, attorney Stillman argued that his client did not intend to cover up the millions of dollars in bonuses he received—and that since there was no criminal intent, there was no fraud. Stillman says Tyco's board of directors knew of and sanctioned the sums. "There was no indication to Swartz that anything was crooked. You have directors who, when something bad happens, all of a sudden have very bad memories," says Stillman. But the jury rejected the argument. The verdict is under appeal.

In the case of former Adelphia finance chief Timothy Rigas, Grand tried to make the case that his client did not know about any wrongdoing at the cable operator. He maintained that the CFO's expanded role at the company following the cancer diagnosis of his father, CEO John Rigas, prevented him from closely monitoring the transactions that were at issue. But again, the jury rejected the argument.

Ebbers, Rigas, and Swartz all received lengthy prison sentences—25 years, 20 years, and $8^{1}/_{3}$ to 25 years, respectively. (All have appealed their convictions.) With criminal prosecution now a common feature of financial investigations, attorneys recognize that the stakes have changed. "If the worst that's going to happen is the guy gets 2 to 3 years in jail, that's tough—it's tough on his family and it's a disgrace," says Keker. "But now, it could be life. It's a lot of pressure."

Billing at rates as high as $700 per hour and taking home paychecks that can run to seven figures, top white-collar defenders are well compensated for handling such pressure. But many say they are in it for more than the money. Keker, for example, relishes the complex legal questions that arise in white-collar defense. "There is always a mental element to a white-collar case," he says. "A lot of these people didn't really think they were committing a crime. They don't think, 'I'm committing a felony,' in the way that someone who sticks a gun in your face and takes your purse knows he's committing a felony."

Such ambiguities keep white-collar practice interesting, agrees Richard Janis. "There's a tendency when you're a prosecutor to think someone is either good or bad," he says. "But in the real world, you can have very good people make a really bad mistake, or you can have people who are unfairly accused."

WEINGARTEN STILL LAMENTS THE OUTCOME OF THE EBBERS TRIAL, WHICH HE HAD ATTEMPTED TO MOVE FROM NEW YORK TO MISSISSIPPI.

In the end, the top white-collar defense lawyers take unpopular and seemingly unwinnable cases like those of the Enron and WorldCom executives simply because somebody has to. "An important part of our criminal justice system is having defense attorneys who will zealously defend their clients. If that wasn't there, the government would run roughshod over people who are innocent," says David Schertler. "That is just as true in white-collar as in traditional street crime." CFO

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REVEALING THE PERSON BEHIND THE NUMBERS

The Human Touch

One of the toughest tasks a defense attorney faces is humanizing a rich, white-collar defendant to a middle-class jury. In the Tyco case, for example, "the bonuses involved were greater than the combined lifetime income of the jury," says Charles Stillman of Stillman & Friedman PC, who defended former Tyco CFO Mark Swartz against fraud and larceny charges. "You have to figure out a way to explain that without offending the people you're talking to."

One technique is to "front the evidence" and deal with the salary and bonus numbers before the prosecution does, say attorneys. "The numbers can be blinding in these cases," says Jeffrey E. Stone, a partner with McDermott Will & Emery in Chicago. To help jurors look beyond outsized pay packages, attorneys explain the responsibilities involved with the CFO role. "You say, 'Yes, this person got paid a lot of money. He got incentive pay because he did a good job,'" says Stone.

Talking about family, philanthropy, and other non-work-related activities can also help a jury warm up to a CFO defendant, says Stone. "It's important that they not be perceived as someone in an austere blue suit who doesn't speak." — K.O'S.

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