

July 18, 2017

Second Circuit Rules that Compliance Monitor's Report is not a Judicial Document, Rejecting District Court's Supervisory Power Over Deferred Prosecution Agreement

On July 12, 2017, the Second Circuit Court of Appeals ruled that a compliance monitor's report, prepared pursuant to a 2012 deferred prosecution agreement ("DPA") entered into between HSBC Bank ("HSBC") and the United States Department of Justice ("DOJ") and filed with the district court, could not be unsealed and made public by the district court.¹ The Second Circuit rejected the district court's ruling that the report was a "judicial" document subject to public disclosure and held that the district court erred in invoking its supervisory authority over the DPA in the absence of a showing of impropriety.²

The Court's decision marks the second time in two years that a federal court of appeals has rejected a district court's attempt to scrutinize a DPA. *See U.S. v. Fokker Servs. B.V.*, 818 F.3d 733 (D.C. Cir. 2016). While the district court's prior opinion approving the DPA after a substantive review, and holding that the court had ongoing supervisory authority to evaluate HSBC's compliance with the DPA, caused speculation about a trend toward greater judicial involvement in DPAs, these recent decisions put an end to that speculation, at least in two circuits. The Second Circuit has made clear that "[a]bsent unusual circumstances . . . a district court's role vis-à-vis a DPA is limited to arraigning the defendant, granting a speedy trial waiver if the DPA does not represent an improper attempt to circumvent the speedy trial clock, and adjudicating motions or disputes as they arise."³

Judge Rosemary Pooler issued a short concurring opinion that was critical of the government's use of DPAs (including nonprosecution agreements) with corporations to "enforce legal theories without such theories ever being tested in court proceedings."⁴ While she acknowledged that "[u]sing DPAs in this manner is neither improper nor undesirable," she suggested that the current use of DPAs with corporations allows prosecutors to "adjudicat[e] guilt and impos[e] sentences with no meaningful oversight from the courts."⁵ She urged Congress to consider enacting legislation that would allow courts to review DPAs.

Whether Congress will step in to address the issues highlighted by Judge Pooler remains to be seen. For the time being, the Second Circuit's ruling means that corporate defendants that enter into DPAs in this circuit should expect that, absent some apparent impropriety, their DPAs will not be scrutinized by the district court. In light of this ruling, federal prosecutors will likely continue to use DPAs as a central tool in resolving corporate criminal investigations, a practice that has increased significantly over the past decade.⁶

The District Court's Prior Rulings

On December 11, 2012, the DOJ filed a criminal information against HSBC in the U.S. District Court for the Eastern District of New York, charging HSBC with anti-money laundering and sanctions violations. That same day, the DOJ and HSBC entered into a DPA in which the DOJ committed to seek the dismissal of the criminal information in five years if HSBC fully complied with the DPA's terms and provisions. Among its terms, the DPA required HSBC to retain a compliance monitor to supervise the bank's remediation and ongoing compliance efforts.

On July 1, 2013, then-Judge Gleeson issued an opinion "approving" the DPA "pursuant to the court's supervisory power," and also ordered the DOJ to file quarterly status reports on the implementation of the DPA.⁷ In its April 2015 status report, the DOJ noted that the compliance monitor had recently completed its First Annual Follow-up Review Report (the "Monitor's Report"), a more substantive document containing an evaluation of the bank's performance under the DPA. Shortly thereafter, the district court ordered the DOJ to file the Monitor's Report with the district court. The DOJ agreed to do so, but requested that the district court accept the filing under seal. Following briefing from HSBC, the DOJ, the compliance monitor, and several other agencies regarding the reasons to maintain the Monitor's Report as a non-public document, the district court agreed to accept the filing under seal.

In November 2015, the district court received a letter from Hubert Moore, a homeowner who had filed a *pro se* complaint against HSBC before the Consumer Financial Protection Bureau after experiencing difficulties in obtaining a mortgage modification. In his letter, Mr. Moore suggested that the Monitor's Report might contain information relevant to his dispute with HSBC. The district court interpreted Mr. Moore's letter as a motion to unseal the Monitor's Report. The DOJ and HSBC filed letters—supported by the monitor, other federal agencies, and certain foreign regulatory agencies—opposing unsealing, arguing that making the Monitor's Report public would impede the monitor's effectiveness and potentially disrupt the cooperation the monitor was receiving from foreign regulators.

On January 28, 2016, the district court ordered that the Monitor's Report be unsealed, with redactions. In reaching its decision, the district court held that the Monitor's Report was a judicial document due to its "relevan[ce] to the performance of the judicial function and useful[ness] in the judicial process," and therefore the court had the power to unseal it.⁸ The district court directed HSBC and the DOJ to propose redactions for the court to consider before unsealing the Monitor's Report.

On March 9, 2016, the district court issued an order directing the implementation of the DOJ's proposed redactions, but also staying the case (and putting on hold the unsealing of the Monitor's Report), pending appellate review. In April 2016, both HSBC and the DOJ sought interlocutory review of the district court's orders.

The Second Circuit's Decision

The Second Circuit began its analysis by observing that “only judicial documents are subject to a presumptive right of public access.”⁹ The Court then considered and rejected the four arguments presented by appellee, Hubert Moore, for holding that the Monitor’s Report was relevant to the district court’s judicial function, and thus qualified as a judicial document.

The District Court's Asserted Supervisory Authority

The Second Circuit recognized a federal court’s ability to exercise its supervisory power over a DPA, acknowledging that there are valid bases for this power; notably, the ability to (1) implement a remedy for violations of recognized rights, (2) preserve judicial integrity by ensuring that a conviction rests on appropriate considerations validly before the jury, and (3) deter illegal conduct. The Court emphasized, however, that this power is an extraordinary one that should be used sparingly.

Turning its attention to the district court’s “novel” basis for applying its supervisory power, the Court observed that the district court’s rationale stood in direct conflict with the “presumption of regularity that federal courts are obliged to ascribe to prosecutorial conduct and decisionmaking.”¹⁰ The Court reasoned that, instead of exercising its supervisory power to prevent any prosecutorial misconduct, the district court was obliged to withhold from exercising its power until it had some indication of actual misconduct. Grounded in these principles, the Court concluded that the district court does not have a “freestanding supervisory power” to “approve” the DPA and monitor its implementation.

The District Court's Power Pursuant to the Speedy Trial Act

Next, the Court considered and rejected appellee’s argument that the Speedy Trial Act provides a district court with the power “to evaluate the substantive merits of a DPA or to supervise a DPA’s out-of-court implementation,” reasoning that there was no evidence that this was Congress’s intent in enacting the federal statute. Considering the somewhat vague text of the statute,¹¹ the Court concluded that Congress would have worded the statute differently if it intended that the Speedy Trial Act provide courts with the power to evaluate the substantive provisions of a DPA. Accordingly, the Court held that the Speedy Trial Act authorizes courts to determine that a DPA is *bona fide* before granting a speedy trial waiver, but does not permit the substantive evaluation of the DPA.

Role of the Monitor Report in Evaluating a Motion to Dismiss or Breach of the DPA

Turning to appellee’s third and fourth arguments, the Court emphasized that even if the Monitor’s Report is relevant to deciding a future motion to dismiss the criminal information or to determining whether there is a breach of the DPA, these bases would not render the Monitor’s Report a judicial document now. The Court likened the Monitor’s Report—a document provided by HSBC to the government—to

documents exchanged in discovery, pointing out that such documents are traditionally beyond the reach of the presumption of public access. The Court explained that an interpretation that such documents could be made public would be a “radical expansion” of the public access doctrine.¹²

The Court emphasized that whether the Monitor’s Report would be useful to the district court in evaluating a future motion to dismiss or alleged breach of the DPA was a speculative exercise that could not support a determination that the Monitor’s Report is presently relevant to the district court’s judicial function.

Judge Pooler’s Concurrence

In a five-page concurrence, Judge Pooler noted that she agreed with the opinion, but she believed that “it is time for Congress to revisit the issue of deferred and nonprosecution agreements.”¹³ Judge Pooler reviewed the Senate Judiciary Committee’s explanation of the Speedy Trial Act, observing that the diversionary nature of DPAs was originally envisioned to help individuals “avoid the collateral consequences of a criminal conviction,” but that, in recent years, they had been used with increasing frequency with corporations.¹⁴ While acknowledging that this use of a DPA was not necessarily inappropriate, Judge Pooler suggested that Congress revisit the purpose of the Speedy Trial Act, and to specifically consider a mechanism for judicial oversight.

Conclusion

The Court’s decision resolves, at least in the Second Circuit, the recent uncertainty surrounding a district court’s authority to supervise a DPA and to make public sensitive documents created as part of a corporate monitorship.

This holding is particularly significant given the increasing prevalence of monitorship requirements in corporate DPAs. The Second Circuit’s opinion makes clear that a district court’s authority to review the substance of the DPA or to monitor its execution and implementation is significantly limited and will remain that way unless, as Judge Pooler urged, Congress determines to give the judiciary a greater role overseeing these agreements.

* * *

This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

H. Christopher Boehning
+1-212-373-3061
cboehning@paulweiss.com

David W. Brown
+1-212-373-3504
dbrown@paulweiss.com

Jessica S. Carey
+1-212-373-3566
jcarey@paulweiss.com

Roberto Finzi
+1-212-373-3311
rfinzi@paulweiss.com

Michael E. Gertzman
+1-212-373-3281
mgertzman@paulweiss.com

Roberto J. Gonzalez
+1-202-223-7316
rgonzalez@paulweiss.com

Brad S. Karp
+1-212-373-3316
bkarp@paulweiss.com

Associates Joseph Delich, Charles J. Hamilton, Katriana G. Roh and Anand Sithian contributed to this Client Alert.

-
- ¹ *U.S. v. HSBC Bank, N.A.*, 16-308(L), slip op. at 6 (2d Cir. July 12, 2017) (hereinafter “*HSBC*”).
- ² We discussed the district court’s decisions to invoke its supervisory authority and to unseal the monitor’s report in prior client memoranda. See “U.S. District Court Applies Supervisory Authority Over Criminal Proceedings to Review of Deferred Prosecution Agreement,” (July 8, 2013), available at https://www.paulweiss.com/media/1705771/8-july-13_alert.pdf; “U.S. District Court Orders Compliance Monitor’s Report Unsealed Pursuant to First Amendment Right of Public Access to Judicial Documents,” (Feb. 1, 2016), available at <https://www.paulweiss.com/media/3333395/1feb2016litalert.pdf>.
- ³ *HSBC* at 6; accord *U.S. v. Fokker Servs. B.V.*, 818 F.3d at 741 (holding that the decision to prosecute—or defer from prosecuting—is the sole responsibility of the Executive Branch through its duty, under Article II, § 3 of the U.S. Constitution, to “take Care that the Laws be faithfully executed.”)
- ⁴ *U.S. v. HSBC Bank, N.A.*, 16-308(L), slip op. at 3 (2d Cir. July 12, 2017) (Pooler, J., concurring) (hereinafter “*HSBC Concurrence*”).
- ⁵ *Id.*
- ⁶ Statistics indicate that since 2000, the DOJ has entered into approximately 330 publicly disclosed agreements (DPAs or NPAs); more than half of these were entered into between 2010 and the end of 2016. See Michael Nagelberg, et al., *Corporate Criminal Liability*, 54 AM. CRIM. L. REV. 1070, 1090 n.119 (Fall 2017).
- ⁷ *U.S. v. HSBC Bank USA, N.A.*, No. 12-CR-763 (JG), 2013 WL 3306161, at *1 (E.D.N.Y. July 1, 2013).
- ⁸ *U.S. v. HSBC Bank USA, N.A.*, 12-CR-763 (JG), 2016 WL 347670, at *2 (E.D.N.Y. Jan. 28, 2016).
- ⁹ *HSBC* at 20.
- ¹⁰ *Id.* at 25.
- ¹¹ The Court noted that “[s]ection 3161(h)(2) excludes from the speedy trial clock ‘[a]ny period of delay during which prosecution is deferred by the attorney for the Government pursuant to written agreement with defendant, with the approval of the court, for the purpose of allowing the defendant to demonstrate his good conduct.’” *Id.* at 28 (quoting 18 U.S.C. § 3161(h)(2) (emphasis in original)).
- ¹² *HSBC* at 33. The Second Circuit noted that a request could be made to the relevant government agencies pursuant to the Freedom of Information Act (“FOIA”), but stated that it was expressing no view as to whether any of FOIA’s exemptions would apply to such a request.
- ¹³ *HSBC Concurrence* at 1.
- ¹⁴ *Id.* at 2.