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THE FALL-OUT FROM THE FINANCIAL CRISIS: CRIMINAL ENFORCEMENT

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Three federal grand jury investigations have been convened in connection with the fall of Lehman Brothers. Twelve Lehman Brothers executives have been subpoenaed. Two managers of a hedge fund affiliated with Bear Stearns were recently charged for allegedly misleading investors about the health of the fund while it was collapsing. In September, a federal grand jury in Brooklyn indicted two former Credit Suisse Group brokers alleging that they lied to investors about how \$1 billion in assets was invested. Fannie Mae, Freddie Mac and American International Group are all reported to be under investigation by the Justice Department as well as by the Securities and Exchange Commission.

The public is looking to hold people and entities responsible for the spectacular collapses of Lehman Brothers, Bear Stearns, and the bail outs necessary for AIG, Fannie Mae and Freddie Mac, among others. The numerous grand juries hurriedly convened reflect the suspicions that criminal wrongdoing may be at the root, at least in part, of the financial crisis.

The Emergency Economic Stabilization Act of 2008 has created the Financial Stability Oversight Board to report to a Special Inspector General or the Attorney General "any suspected fraud, misrepresentations or malfeasance." The Act also requires that any federal financial regulatory agency cooperate with the FBI on investigations involving "fraud, misrepresentations and malfeasance with respect to development, advertising and sale of financial products."

It is likely that these investigations will not only be centered on financial institutions and their executives. Rather, all companies that experience a huge drop in value attributable in whole or in part to their investment in subprime mortgages, derivatives, or other "risky" investments, are likely to draw the attention of disgruntled shareholders, regulators, and possibly the criminal authorities. The climate and Congressional response to date are very reminiscent of the Office of Thrift Supervision and the Resolution Trust Corporation response to the savings and loan crisis of the late 80s and early 90s.

With the public's thirst for retribution, the focus initially will be on financial institutions and their

officers and directors. More specifically, the issue will be whether the government can prove a case beyond a reasonable doubt of criminal wrongdoing, as opposed to mistakes in judgment and negligence.

It is also likely that criminal investigations will be paired with civil lawsuits, either from angry shareholders or regulatory authorities, such as the SEC and the Office of Financial Stability. Defendants likely will be faced with difficult decisions to navigate through the thicket of parallel proceedings, with the spectre of potential criminal proceedings looming.

What To Do

There are numerous steps that companies can take to be proactive.

- Scrutinize disclosures and financial statements for possible misstatements.

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- Conduct an internal investigation, including an email review, into alleged wrongdoings.
- Review and revise corporate provisions for indemnification of officers and directors.

Lowenstein Sandler's White Collar Criminal Defense Practice Group is one of the deepest and most experienced groups in the country. The Group has handled, in recent years, more than 50 major securities fraud prosecutions nationwide. It also has the experience of having handled numerous investigations and defense of financial institutions and their executives dating back to the savings and loan crisis of the late 80s and early 90s.

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